

Developing RMB products in Hong Kong Speech at CPA Congress

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Introduction

Good afternoon ladies and gentlemen. It's my pleasure to be here today and may I first thank the organisers, CPA, for their invitation.

The topic I have today is "Developing RMB products in Hong Kong". I thought that rather than focusing on a narrow topic, I should step back and paint for you a broader landscape of the co-operative relationship between the Mainland and Hong Kong financial markets, in particular the role that Hong Kong plays in this regard. This will provide the context within which to understand the development of renminbi (RMB) products.

Co-operative relationship between the Mainland and Hong Kong financial markets

The co-operative relationship between the Mainland and Hong Kong financial markets is an important one. The principle of "one country two systems" has been vital to Hong Kong's stability and its continued development and success as an international financial centre.

How Hong Kong can help?

As the Mainland enters the world's economic stage, Hong Kong has a meaningful role to play in facilitating and supporting the Mainland in her journey. Hong Kong is blessed to have been a recipient of the benefits from the opening up of the Mainland market. In fact, we have the first mover advantage. In return, we have something valuable to offer. Hong Kong has the qualities to help the Mainland to become an international success. Hong Kong's strengths lie in its superior infrastructure, sound legal system and open architecture. There are two aspects to this.

First, Hong Kong can and should offer to share its experience, knowledge and expertise with relevant Mainland players to help them build capabilities. By sharing and working closely with the Mainland, we develop better and wider business opportunities. For example, the fund raising by Mainland enterprises, the gradual implementation of Qualified Domestic Institutional Investor (QDII) programme, and certain securities-related initiatives under the Closer Economic Partnership Arrangement (CEPA) are designed to give the Mainland issuers, financial intermediaries, and investors first-hand experience in operating in the open and international environment of Hong Kong. In return, Mainland players and investors have brought tremendous opportunities to Hong Kong.



Second, Hong Kong is positioned as a testing ground for reforms and measures to open up avenues for trading and investment in RMB. Hong Kong's strategic value to the Mainland lies in its status as an international offshore market, a place where the Mainland can conduct capital market experiments in a market separated from the Mainland market and in an environment that operates on international rules.

Transformation of Hong Kong's role

Throughout the years, Hong Kong has transformed its role in that not only does it act as the prime overseas fund-raising centre for Mainland enterprises, it also acts as an investment platform for Mainland investors. This journey has been an exciting one. Let me explain.

Hong Kong has developed into a prime overseas fund-raising centre for Mainland enterprises. At the same time, the Mainland market, with its enormous demand for financial services, has given impetus to Hong Kong's financial development. The metamorphosis that saw Hong Kong's market develop from a domestic market into an international market began in 1993, when the first H-share company was listed in Hong Kong. Since then, we have helped H-share and red chip companies and minying enterprises raised a total of HK\$2,739 billion in the Hong Kong market, HK\$1,486 billion of which was raised through initial public offerings (IPOs) and HK\$1,253 billion of which was raised through secondary offerings. Today, international and institutional investors have continued to regard Hong Kong as the preferred market for them to invest directly in Mainland companies. 60% of our market turnover is from institutional and international money. Despite the uncertainty over the recovery in many of the world's developed economies, in 2009, Hong Kong ranked number one globally for IPO fund-raising (HK\$248 billion), and number four globally in total funds raised (HK\$642 billion). This year, including the listing of AIA Group Limited today, Hong Kong is once again the largest IPO market worldwide, having raised HK\$330 billion to date. The Hong Kong IPO market would not have been such a success without the help of you all, the accountants and auditors who are one of our key gatekeepers in helping to keep the quality of our market. Let me take this opportunity to thank all of you for your hard work, professionalism and dedication.

Hong Kong also acts as an investment platform providing opportunities for Mainland investors to access the international markets. An example is overseas direct investments (ODI). During the first half of 2010, ODI reached US\$22.4 billion, rising 55% as compared to the same period in 2009. It was reported that the Mainland authorities are studying the possibility to launch ODI in RMB on a trial basis. Such new measures are expected to significantly broaden the scope of Hong Kong's financial services, taking advantage of Hong Kong's being the primary investment hub accommodating about 60% of the Mainland's ODI.

Recent development in the investment product market in Hong Kong

Let me share with you the recent developments in the investment product market in Hong Kong, highlighting some of the key regulatory changes in this area, together with the development of RMB products in Hong Kong.

Regulatory changes in Hong Kong

We have recently revisited our requirements for certain investment products that are offered to the public in Hong Kong. The revisions covered funds, unlisted structured investment



products and investment-linked assurance schemes. There were also changes to the conduct requirement for intermediaries to enhance selling practices relating to the sale of investment products. These measures were broad-ranging and were directed at enhancing investor protection and addressing some of the issues that have arisen as a result of the financial crisis. Nevertheless, we were mindful that any regulatory response needed to be measured without unduly stifling the market.

A key measure introduced earlier this year is the requirement that issuers of retail investment products must prepare a product key facts statement or what we call a “KFS”. A KFS is a short, user-friendly document summarising the key features, risks and costs of a product. The key objectives - brevity, clarity and comparability - aim to make it easier for investors to understand and compare different products. However, a KFS is not intended to replace the offering document of an investment product. We have started to implement the KFS requirement. The industry has made good efforts to meet the new requirements. The feedback from investors has been positive. We will continue to work closely with the industry to ensure a smooth implementation of the KFS regime.

Recently, there are rumours in the market that the Securities and Futures Commission (SFC) will not authorize synthetic exchange-traded funds (ETFs). This is not true. In fact, synthetic ETFs have provided investors with a wider range of investment opportunities and choices, in particular the opportunity of investing in a relatively easy manner in markets otherwise restricted to them. As well, these ETFs have helped develop the strength, volume and reputation of Hong Kong's ETF platform. We would like to be able to continue to authorize these products.

The SFC has noted that the public may not be fully aware of the difference between traditional physical ETFs and synthetic ETFs. The SFC is working with the Stock Exchange of Hong Kong and we are in dialogue with the industry on measures to help investors better differentiate the two and to increase product transparency. For instance, we will encourage the industry to prepare KFS as soon as possible so that investors would be provided with clear, succinct and useful disclosure. We believe this will enable easier reading and comparison among investment products. With a view to enhancing the transparency of synthetic ETFs and given that the internet is now an important channel of communication with investors trading listed securities, we are working with ETF managers to see whether and how the website disclosure could be further enhanced.

Further, a good amount of investor education work has been done and will continue to be done to keep investors educated, informed and alert to the risks of investing in synthetic ETFs.

Expansion of the investment product market in Hong Kong

The range of investment products available to retail investors has continued to grow. For example, we authorized the first ETF managed by the Hong Kong asset management subsidiary of a Mainland insurance group in April this year. More recently, in October this year, we authorized the first gold ETF managed by a local manager with the gold kept in a vault in Hong Kong. This brings the total number of ETFs listed in Hong Kong to 67. This reaffirms Hong Kong's position as the second-largest ETF market in Asia. In the space of real estate investment funds (REITs), SFC-authorized REITs marked a new milestone. In April this year, when a Singapore-listed REIT was listed on the Stock Exchange of Hong Kong by way of



introduction. We welcome issuers to come in to discuss their plans for new products. Our doors are always opened.

RMB investment products

Let me now discuss RMB investment products, an area which has generated much interest. The recent developments in RMB business are significant for the Hong Kong market, not only in terms of the rapidly growing volume, but also in the wider range of investment products available to investors in Hong Kong. Since the announcement of a series of measures earlier this year to relax the restrictions over the conduct of offshore RMB business, the total amount of RMB deposits in Hong Kong rose to RMB130.4 billion as of end August 2010, more than double the RMB62.7 billion at the end of 2009. Of course, relative to the RMB68.75 trillion of China's M2, our deposit pool is insignificant. Yet, it underscores the strong interest in and growth prospects of RMB as a currency on the ascent.

With corporates being allowed to open RMB accounts for any general purposes, and funds being able to transfer among RMB accounts in Hong Kong for any purpose, the scope for designing RMB investment products has broadened in Hong Kong. There are now different types of investment products that can be issued in RMB, these include: bonds, certificates of deposits, structured deposits, insurance policies and funds, etc.

In the space of RMB-denominated bonds, the growth has been encouraging. Hong Kong started developing an offshore RMB bond market in 2007. As of 21 October 2010, the total amount of RMB bonds issued in Hong Kong stood at RMB50.78 billion. The universe of issuers includes not only Mainland Chinese banks but also Hong Kong banks and corporations and foreign corporations. For example, McDonald's Corporation, based in the US, issued RMB200 million notes in a private placement to Hong Kong institutional and professional investors to support its growth in China in August 2010. Recently on 22 October, the RMB-denominated bond issued by the Asian Development Bank, worth RMB1.2 billion, debuted on the Hong Kong stock exchange, making it the first exchange-traded RMB-denominated/settled bond in Hong Kong.

In August this year, we authorized the first RMB-denominated fund for public distribution in Hong Kong with subscriptions and redemptions settled in RMB. The fund assets are primarily intended to be invested in RMB-denominated debt instruments issued outside the Mainland. In fact, in October this year, we authorized a second RMB-denominated fund, sharing features similar to that I have just talked about. We expect a wider range of fund products to come to market as the universe of RMB assets available in or to Hong Kong continues to grow.

The development of RMB products in Hong Kong will continue to attract RMB liquidity to Hong Kong. Of course, at this experimentation stage, the offshore RMB business should serve the needs of the growth of the Mainland economy and its foreign trade. We should therefore approach all new RMB investments products with caution, vigilance and care. Issuers must put their clients' interests first. Further, investors need to understand the features and risks of this new range of investment products. In this respect, the SFC will continue to work on investor education initiatives to arouse awareness, and to help investors better understand the features and risks inherent in RMB investment products.



Closing remarks

The Mainland is poised to become a player in the new world financial order. Hong Kong is key partner in that journey. We will continue to work closely with the industry and all relevant parties to foster deeper ties and broader opportunities with the Mainland. The breadth and depth of the investment products market in Hong Kong have grown in recent years. This is an exciting journey with many opportunities that lie ahead. You have all helped to make this happen and I am very pleased that you are on board this journey with us. I hope you will join us on board to take this journey to further and greater success.

Thank you.