



SECURITIES AND FUTURES COMMISSION
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Research Paper No. 56: A Review of the Global and Local Securities Markets in 2014

16 January 2015



Executive summary

1. In the US, the Dow, S&P and Nasdaq rose 7.5%, 11.4% and 13.4% respectively during 2014. After gaining some 30% in 2013, the US market continued to rise on optimism about economic recovery and corporate earnings. The commitment of the US Federal Reserve Bank (Fed) to a low interest rate provided support. The Dow and S&P rose to record highs whilst the Nasdaq rose to its highest level in 14 years.
 2. In Europe, the FTSE and CAC fell 2.7% and 0.5% respectively, whilst the DAX rose 2.7%. A dim economic outlook and deflation concerns persisted. Losses were trimmed due to the European Central Bank's policy to adopt negative deposit rates and cut its benchmark interest rate.
 3. In Asia, the Nikkei 225 Index, which had surged 56.7% in 2013, rose 7.1% in 2014 to hit a seven-year high after the Bank of Japan announced massive stimulus. The weaker yen paced gains. The performance of other major regional markets was mixed, ranging from a 5.7% loss in Malaysia to a 31.4% increase in India.
 4. In the Mainland, the Shanghai Composite Index rose 52.9%, making the Mainland market one of the best performing markets worldwide. The Mainland market rose on hopes for supportive government policies. Expectations for more state-owned enterprise reforms and increases in infrastructure spending paced gains. In November, the People's Bank of China (PBoC) unexpectedly cut interest rates, the first time in more than two years. The market rallied to an almost five-year high of over 3,200 points in active trading. Total daily trading on the Shanghai and Shenzhen stock markets rose to a historical high of over RMB1 trillion in early December.
 5. In Hong Kong, the Hang Seng Index (HSI) and the Hang Seng China Enterprises Index (HSCEI) rose 1.3% and 10.8% respectively, compared to a respective rise of 2.9% and decline of 5.4% in 2013. At one point, the HSI rose to a six-year high of over 25,000 points, tracking the rally in the Mainland market. Despite strong rallies in the US and Mainland markets, concerns over the Fed's tapering and an uncertain Mainland economic outlook weighed on the Hong Kong market.
 6. Some of the major risks and uncertainties facing the Hong Kong market include:
 - valuation concerns in the US and Mainland markets;
 - worries about interest rate hikes in the US;
 - lingering macro risks despite central banks' measures to inject liquidity into major markets; and
 - pressures on regional currencies amid a depreciating yen.
 7. Trading in both the cash market and exchange-traded derivatives rose. The average daily trading in the cash market rose 11%. Trading in futures products fell 3%, whilst that in options products rose 16% from the 2013 level.
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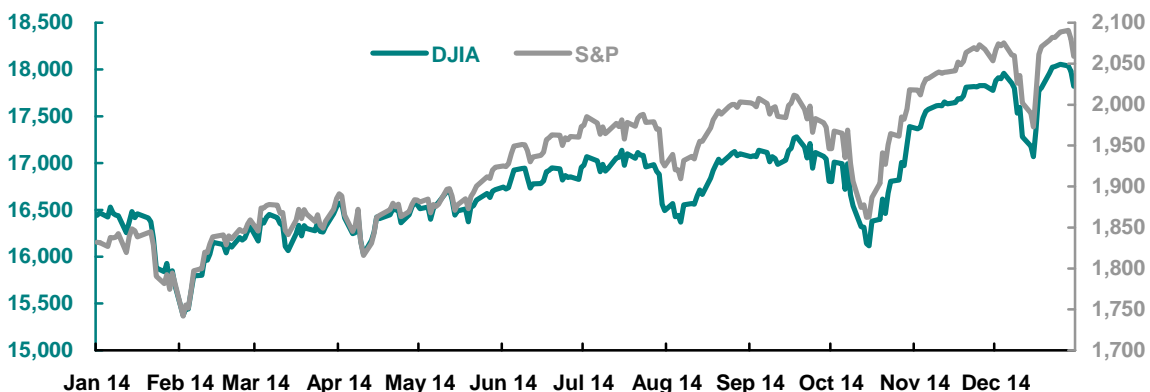


Performance of stock markets during 2014

8. During 2014, most major markets rose on optimism about supportive government measures. In early 2014, concerns about the Fed's tapering and uncertainties about the global economic outlook weighed on the markets. Later, most markets recovered on the back of upbeat economic data and better corporate earnings. In late 2014, while the Fed ended stimulus measures smoothly, the central banks in Europe, Japan and the Mainland adopted monetary easing policies, providing support to the global stock markets.

The US

9. After gaining some 30% in 2013, the US market continued to rise in 2014 as the Dow, S&P and Nasdaq rose 7.5%, 11.4% and 13.4% respectively on optimism about economic recovery and corporate earnings. The Dow and S&P reached record highs whilst the Nasdaq also rose to its highest level in 14 years.
10. In early 2014, the US market was volatile following the start of the Fed's tapering. Since December 2013, the Fed began to reduce its monthly bond purchase by US\$10 billion each time from US\$85 billion. Investors were worried that the withdrawal of stimulus might hurt the fragile economic recovery and corporate earnings. This triggered some sell-off in emerging market assets amid concerns about a withdrawal of liquidity.
11. Losses were recouped later as emerging market currencies stabilised somewhat after certain central banks raised interest rates. Upbeat earnings and solid economic data also provided support. However, heightened tensions in Iraq trimmed gains.
12. In early October, the market corrected on worries over the global economic outlook. The International Monetary Fund cut its global growth forecast for the third time since the beginning of the year. The diagnosis of Ebola cases in the US also hurt investor sentiment.
13. In late October, the Fed's stimulus program ended as expected. Though the timing of interest rate hikes remained uncertain, the Fed reassured that it would keep interest rates low for a considerable period of time. It also indicated confidence in the pace of economic recovery.
14. The Dow and S&P 500 rose to fresh record highs as the Republicans won control of the Senate in mid-term election during November. Solid jobs and housing data paced gains.
15. However, the market became choppy in December given concerns about contagion from the correction in the Russian market. Amid declining oil prices, Russia, as a major oil exporter, saw its stock market and currency both drop sharply. Later, the Russian situation stabilised somewhat and the US market rose strongly after the Fed stated that it would not raise interest rates in the near future.



Performance of DJIA and S&P during 2014

Source: Bloomberg



Performance of major stock markets

		End-2014	% change			PE Ratios
		Index Level	2014	2013	2012	End-2014
Hong Kong and the Mainland						
HK	-HSI	23,605.04	1.3%	2.9%	22.9%	9.98
	-HSCEI	11,984.69	10.8%	-5.4%	15.1%	8.38
Mainland	-Shanghai Comp	3,234.68	52.9%	-6.7%	3.2%	15.45
	-Shenzhen Comp	1,415.19	33.8%	20.0%	1.7%	34.36
Asia						
Japan	-Nikkei 225	17,450.77	7.1%	56.7%	22.9%	21.39
Australia	-AOI	5,388.60	0.7%	14.8%	13.5%	20.43
Taiwan	-TWSE	9,307.26	8.1%	11.8%	8.9%	15.39
Korea	-KOSPI	1,915.59	-4.8%	0.7%	9.4%	29.25
Singapore	-STI	3,365.15	6.2%	0.0%	19.7%	13.65
Thailand	-SET	1,497.67	15.3%	-6.7%	35.8%	9.79
Malaysia	-KLCI	1,761.25	-5.7%	10.5%	10.3%	15.78
Indonesia	-JCI	5,226.95	22.3%	-1.0%	12.9%	20.96
India	-Nifty	8,282.70	31.4%	6.8%	27.7%	19.02
Philippines	-PCOMP	7,230.57	22.8%	1.3%	33.0%	20.83
Vietnam	-VN	545.63	8.1%	22.0%	17.7%	13.28
US						
US	-Dow	17,823.07	7.5%	26.5%	7.3%	15.92
	-Nasdaq	4,736.05	13.4%	38.3%	15.9%	42.06
	-S&P	2,058.90	11.4%	29.6%	13.4%	18.22
Europe						
UK	-FTSE100	6,566.09	-2.7%	14.4%	5.8%	18.78
Germany	-DAX	9,805.55	2.7%	25.5%	29.1%	17.22
France	-CAC	4,272.75	-0.5%	18.0%	15.2%	25.55
PIIGS and Hungary						
Portugal	-PSI20	4,798.99	-26.8%	16.0%	2.9%	N/A
Italy	-FTSEMIB	19,011.96	0.2%	16.6%	7.8%	N/A
Ireland	-ISEQ	5,224.56	15.1%	33.6%	17.1%	34.44
Greece	-ASE	826.18	-28.9%	28.1%	33.4%	N/A
Spain	-IBEX	10,279.50	3.7%	21.4%	-4.7%	21.63
Hungary	-BUX	16,634.00	-10.4%	2.2%	7.1%	N/A
Middle East and North Africa						
Egypt	-EGX30	8,926.58	31.6%	24.2%	50.8%	N/A
Dubai	-DFMGI	3,774.00	12.0%	107.7%	19.9%	11.07
Other BRIC markets						
Brazil	-IBOV	50,007.41	-2.9%	-15.5%	7.4%	16.32
Russia	-MICEX	1,396.61	-7.1%	2.0%	5.2%	7.32

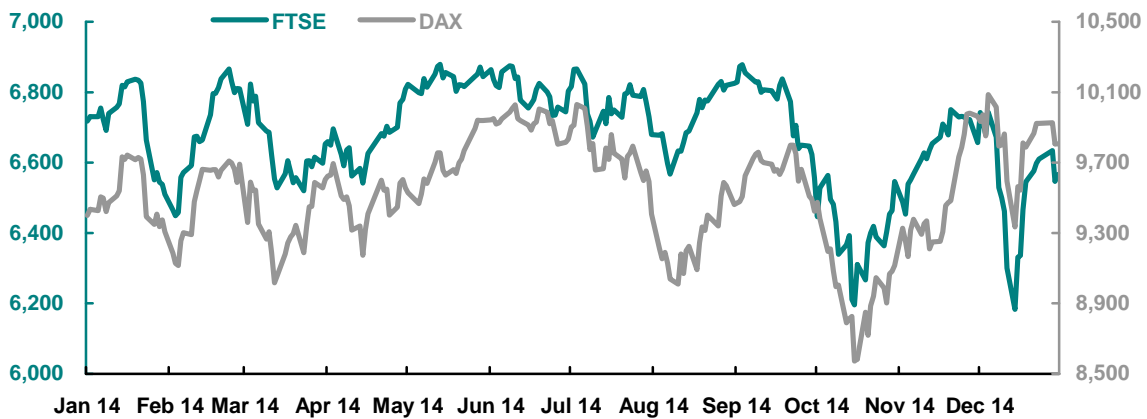
Source: Bloomberg

Europe

- In 2014, the FTSE and CAC fell 2.7% and 0.5% respectively, whilst the DAX rose 2.7%, after recording gains of 14.4%, 25.5% and 18.0% respectively in 2013. The DAX once rose to a record high.
- European markets were volatile amid uncertainties over economic growth in the Eurozone economy. The European Central Bank (ECB) adopted negative deposit rates in June and cut its benchmark interest rate by 10 basis points to 0.05% in September. The measures provided some short-term boost to European markets. However, uncertainties remained and concerns over a dim economic outlook in Europe lingered. Eurozone economic data were largely weaker than expected.



18. In late July, Standard & Poor's downgraded Argentina's credit rating to selective default. Concerns about financial stress in the Portuguese banking sector paced losses. Ongoing geopolitical tensions in Russia and Ukraine and uncertainties during the Scottish referendum on independence also weighed on market sentiment.
19. In October, the markets retreated as deflation concerns persisted and investors were disappointed at the timing and size of further monetary easing measures from the ECB. Worries over the debt problem revived. Bond yields of peripheral Eurozone countries rose amid worries about the pace of economic recovery in Greece.
20. The ECB's plans to inject liquidity into the Eurozone economy recouped some losses before the markets dipped again in December, as worries over the market situations in Russia intensified amid a slump in the Russian ruble and crude oil prices. The markets also paced losses on uncertainties over the continuation of the Greek bailout plan after its government unexpectedly advanced the presidential election. Sovereign credit rating downgrades of Italy and France, by Standard & Poor's and Fitch respectively, dragged the markets lower. However, the markets rebounded somewhat towards the end of the year as the Bank of Spain forecasted more rapid growth and Portugal's budget deficit declined.

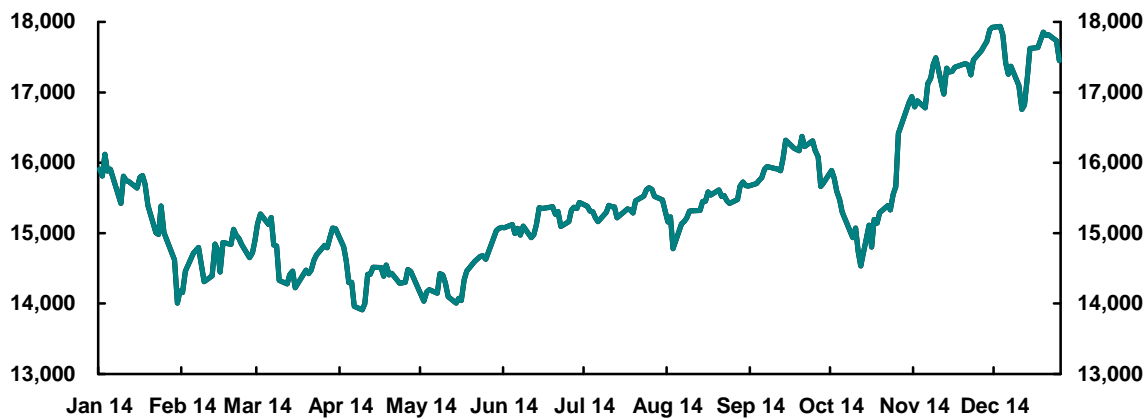


Performance of FTSE and DAX during 2014

Source: Bloomberg

Asia

21. In Japan, the Nikkei 225 Index rose 7.1% in 2014, after rising 56.7% in 2013. In early 2014, the market fell on worries that the sales tax hike in April might dampen economic growth and corporate earnings. A stronger yen paced losses. However, the market later rebounded gradually on hopes for more supportive government measures. In December, the Nikkei 225 Index rose to a seven-year high, despite a downgrade of Japan's sovereign debt rating by Moody's. Investors were optimistic about the economic outlook after Prime Minister Abe's ruling party won the election. The Bank of Japan announced massive stimulus and the Government Pension Investment Fund indicated its plan to buy more domestic shares. The yen slid to a seven and a half year low. A delay in the second sales tax increase also lent support.
22. The performance of other major regional markets was mixed in 2014, ranging from a 5.7% loss in Malaysia to a 31.4% increase in India. The military coup in Thailand seemed to have limited impact on regional markets.

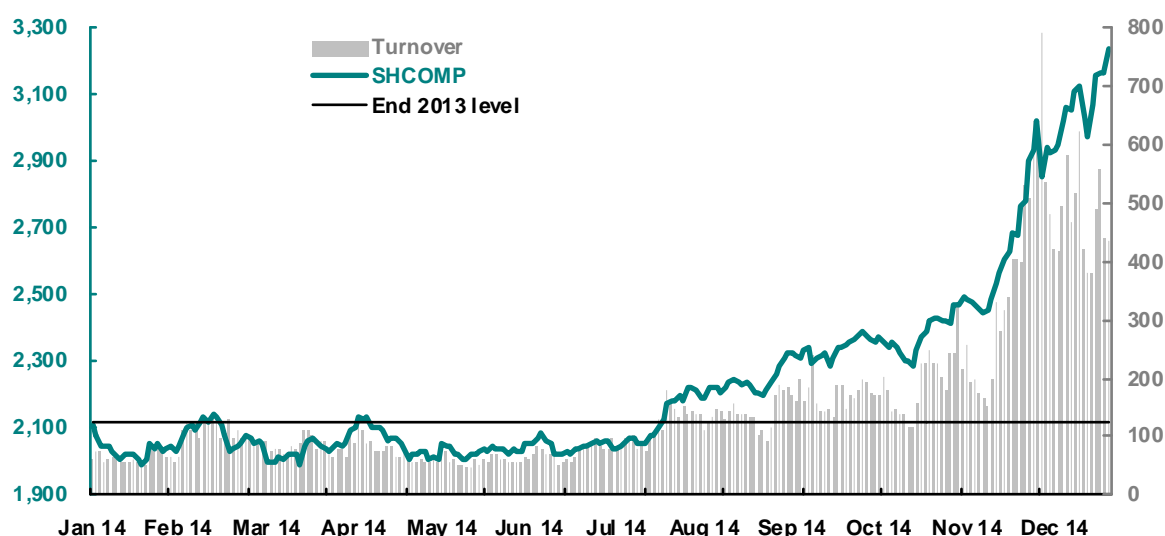


Performance of Nikkei 225 during 2014

Source: Bloomberg

The Mainland

23. Following a fall of 6.7% in 2013, the Shanghai Composite Index rose 52.9% in 2014, making the Mainland market one of the best performing markets worldwide. Trading was active, and total daily trading on the Shanghai and Shenzhen stock markets rose to a historical high of over RMB1 trillion in early December.
24. In early 2014, the market was volatile on lingering liquidity concerns amid worries over the resumption of initial public offerings (IPOs). There were uncertainties about a slowdown in economic growth given mixed economic data. Concerns about credit risks heightened amid default cases of corporate bonds and wealth management products.
25. From July, the market rebounded on hopes for supportive government policies. The People's Bank of China (PBoC) announced measures to support smaller companies and cut the reserve requirement ratio for qualified banks. In September, it injected liquidity to major banks through the Standing Lending Facility. Expectations for more state-owned enterprise reforms and the possible expansion of free trade zone projects paced gains.
26. In early November, investor sentiment became more bullish as President Xi Jinping announced a plan to accelerate the construction of the Silk Road Economic Belt, boosting hopes for an increase in infrastructure spending.
27. In late November, the PBoC unexpectedly cut interest rates for the first time in more than two years. Amid hopes for supportive measures, including further cuts in the interest rate or reserve requirement ratio, the market rallied to an almost five-year high of over 3,200 points. Financial and infrastructure sectors, which benefited from supportive government policies, contributed most to the gains. Large-cap stocks outperformed. Amid bullish sentiment, margin financing rose to a record high, boosting trading activities.



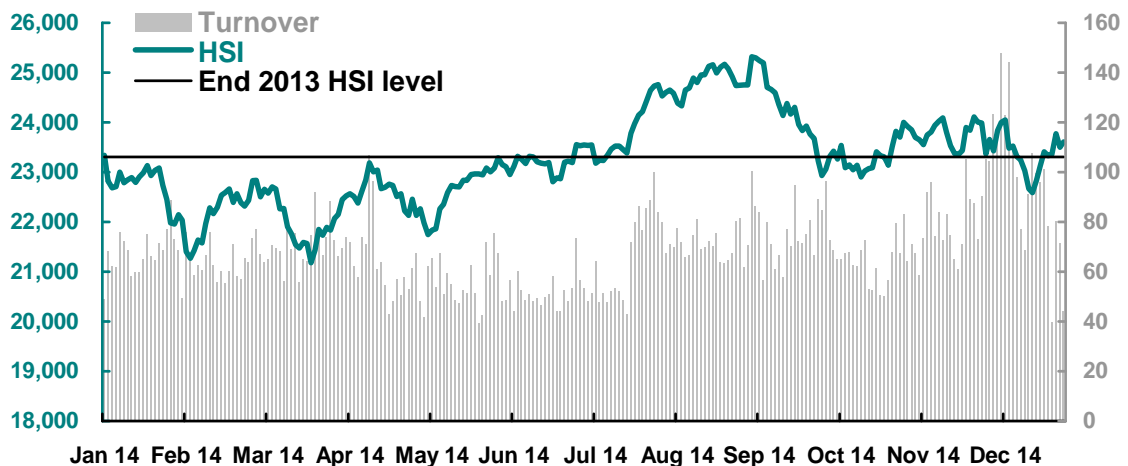
**Shanghai Composite Index and
Shanghai Market Turnover (RMB billion) during 2014**

Source: Bloomberg

Hong Kong

28. In 2014, the HSI and the HSCEI rose 1.3% and 10.8% respectively, following a respective increase of 2.9% and fall of 5.4% in 2013. Concerns over the US Fed's tapering and uncertain Mainland economic outlook weighed on the market.
29. In early 2014, the Hong Kong market was choppy amid concerns about the Fed's withdrawal of stimulus policies and economic uncertainties in emerging markets. Worries about an economic slowdown in the Mainland and geopolitical tensions in Ukraine lingered. In early April, the announcement of Shanghai-Hong Kong Stock Connect (Stock Connect) lifted market sentiment. Optimism over the Mainland government's stimulus measures and state-owned enterprise reforms lent some support.
30. Later, the market rose on an improved global economic outlook and robust performances in major overseas markets. Huge capital inflows to the Hong Kong market also paced gains. In July, the Hong Kong Monetary Authority bought US\$8.3 billion (equivalent to \$65 billion¹) to meet the strong demand for the Hong Kong dollar.
31. In early September, the HSI hit a six-year high of over 25,000 points, tracking the rally in the Mainland market. Optimism in the global economic outlook paced gains. In November, Stock Connect was launched and market sentiment improved following an interest rate cut in the Mainland. Later, the market trimmed some earlier gains on concerns about global economic outlook.
32. In early December, the HSI and the HSCEI advanced amid a rally in the Mainland market. H-shares outperformed. Trading was active. Later, the market gave up some gains amid a sharp decline in oil prices and heightened volatility in the Russian market. In late December, market sentiment was lifted as the US and Mainland markets rallied.

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



HSI and Hong Kong Market Turnover (\$ billion) during 2014

Source: Bloomberg

Risks and uncertainties facing the Hong Kong market

33. In 2014, the Hong Kong market was volatile as it was affected by both overseas and Mainland market conditions. Looking forward, the market may face risks and uncertainties including:
- Valuation concerns in the US and Mainland markets – The US stock market has accumulated substantial gains and hit many record highs. The Mainland market also experienced a strong rally after an interest rate cut in November. Investors are cautious whether economic growth and corporate profits can sustain further increases in valuations. Investor sentiment has become more fragile when faced with disappointing news concerning economic performance or policy changes. Markets are vulnerable to higher volatility.
 - Uncertainties over US interest rate hikes – Despite the Fed's commitment to keep interest rates low for a considerable period of time, signs of improvement in economic conditions may trigger an earlier-than-expected rate hike. A change in monetary policy will affect the global economic and stock market outlook and cause a shift in fund flows amongst different markets and asset classes.
 - Global macro risks – Major central banks in Europe, Japan and China announced supportive policies in face of uncertain economic conditions. Time will tell if these measures succeed in reviving their respective markets. In Europe, economic recovery remains fragile and worries over deflation linger. Japan still faces risk of a recession despite continued stimulus measures. There are also concerns about whether the Mainland economy can sustain high and balanced growth. It is uncertain to what extent the injection of liquidity by central banks in their markets would be able to offset the impact of future US interest rate hikes on economy.
 - Pressures on regional currencies – Japan's loose monetary policy has put pressure on the yen. This has raised concerns regarding competitive devaluations of other Asian currencies as had happened during the Asian Financial Crisis. Given the improvements in their current account and credit conditions, Asian economies today are better positioned to withstand certain shocks. However, the recent volatility of the Russian market still caused worries about contagion effects on emerging markets and their currencies.



Major statistics of Hong Kong securities market in 2014

Trading activity in the local stock market

34. Trading in the local stock market increased. In 2014, the average daily turnover amounted to \$70 billion, 11% higher than the \$63 billion level in 2013.
35. Mainland stocks remained the most actively traded. Their share of total market turnover was 37% in 2014 (39% in 2013), while HSI stocks (excluding H-shares and red chips) accounted for about 17% (16% in 2013).

Average Daily Turnover (\$ billion)

	2014		2013		% change over 2013
HSI (ex H shares & red chips)	12.1	(17%)	9.8	(16%)	+23%
Mainland Stocks	25.5	(37%)	24.3	(39%)	+5%
<i>H-shares</i>	17.8	(26%)	17.3	(28%)	+3%
<i>Red chips</i>	7.7	(11%)	7.0	(11%)	+10%
Derivative Warrants	8.3	(12%)	7.3	(12%)	+13%
CBBCs	5.0	(7%)	5.2	(8%)	-4%
ETFs	4.7	(7%)	3.7	(6%)	+28%
Others	13.9	(20%)	12.3	(20%)	+13%
Market Total	69.5	(100%)	62.6	(100%)	+11%

Remark: Percentages in parenthesis denote market share.

Sources: Hong Kong Exchanges and Clearing Limited (HKEx) and SFC Research

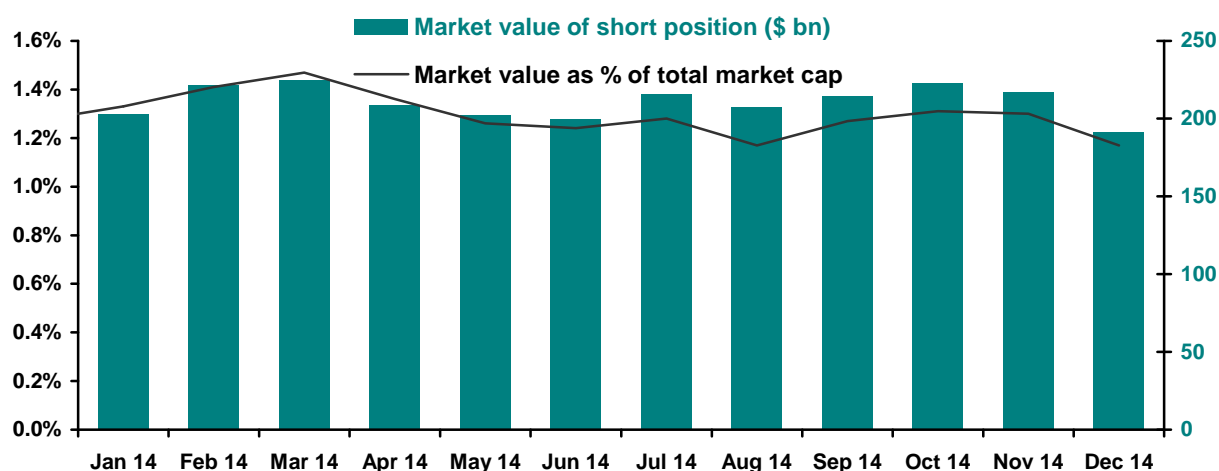
Stock Connect

36. Stock Connect was launched on 17 November 2014 to provide mutual trading access between the Shanghai and Hong Kong stock markets. The Shanghai Stock Exchange and HKEx enable investors to trade eligible shares listed on the other's market subject to quota.
37. The northbound daily quota is set at RMB13 billion, and the southbound daily quota is set at RMB10.5 billion.
 - The northbound daily quota was used up on 17 November 2014, the launch date. Afterwards, northbound daily quota usage ranged between RMB0.7 billion (5.0%) – RMB7 billion (53.5%).
 - The southbound daily quota usage ranged between RMB0.1 billion (1.3%) – 1.8 billion (16.7%).
38. The northbound aggregate quota is set at RMB300 billion, and the southbound aggregate quota is set at RMB250 billion. As of 31 December 2014, cumulatively:
 - the northbound aggregate quota usage was RMB74.6 billion (24.9%); and
 - the southbound aggregate quota usage was RMB10.5 billion (4.2%).
39. As of 31 December 2014, there were 569 eligible stocks for northbound trading and 273 eligible stocks for southbound trading. During 17 November 2014 – 31 December 2014:
 - Northbound average daily trading was RMB5.6 billion or 0.7% of Mainland market trading. Most of the actively traded stocks were large-cap stocks and AH stocks with A-shares traded at discount to H-shares.
 - Southbound average daily trading was RMB0.8 billion or 0.5% of Hong Kong market trading. Most of the actively traded stocks were AH stocks and Mainland private enterprises.



Short-selling activity

40. Compared to 2013, short selling was higher in both absolute terms and as a percentage of total market turnover. The average daily short selling was \$7.2 billion, or 10.3% of total market turnover in 2014. In 2013, the average daily short selling was \$6.1 billion, or 9.8% of total market turnover.
41. Based on the data submitted, as at 24 December 2014, aggregated short positions amounted to \$191 billion (or 1.2% of the market cap of the reported stocks).



Sources: HKEx and SFC Research

Initial public offerings

42. There were 115 initial public offerings (IPOs) in Hong Kong in 2014. IPO funds raised totalled \$232.5 billion. This compared to 102 IPOs (\$169.0 billion) in 2013. IPO funds raised by Mainland companies accounted for 86% of the market total during 2014. Hong Kong ranked the second in IPO activities worldwide both in 2014 and 2013.

Top 10 Stock Markets in the World, by Equity Funds Raised through IPOs (2014)

	Equity Funds Raised through IPO		
	US\$ billion	Worldwide Ranking	Asia Ranking
US (NYSE Euronext)	74.3	1	-
Hong Kong	30.0	2	1
UK (London)	27.3	3	-
US (Nasdaq OMX)	24.5	4	-
Australia	16.0	5	2
Japan (Tokyo)	11.5	6	3
Euronext - Amsterdam	9.1	7	-
China (Shenzhen)	7.3	8	4
Saudi Arabia (Tadawul)	6.7	9	-
Spain (Madrid)	6.5	10	-

Remarks: Data is provisional only.

Source: HKEx



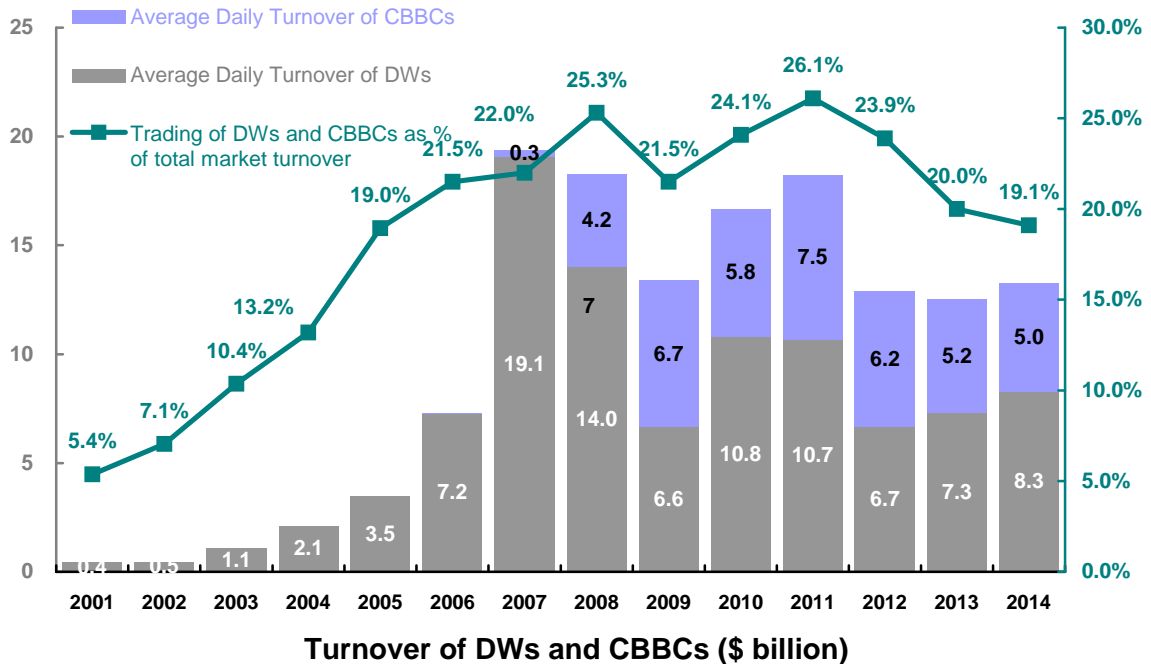
Exchange-traded funds

43. The number of exchange-traded-funds (ETFs) rose to 122 as at end-2014 from 116 as at end-2013. Their average daily turnover was \$4.7 billion in 2014, which was 27% higher than the \$3.7 billion in 2013. ETFs accounted for 7% of total market turnover in 2014 (compared to 6.0% in 2013). The average daily turnover of A-shares ETFs was \$3.6 billion, contributing to 76% of total ETF turnover (compared to \$2.7 billion and 74% in 2013).

Derivatives warrants and callable bull/bear contracts

44. In 2014, trading of derivatives warrants (DWs) increased in absolute terms and as a percentage of the total market turnover. The average daily turnover of DWs rose to \$8.3 billion (11.9% of total market turnover), compared to \$7.3 billion (11.7% of total market turnover) in 2013.

45. In 2014, trading in callable bull/bear contracts (CBBCs) decreased in both absolute terms and as a percentage of the total market turnover. The average daily turnover of CBBCs decreased to \$5.0 billion (7.2% of total market turnover), compared to \$5.2 billion (8.3% of total market turnover) in 2013.



Source: SFC Research

Exchange-traded derivatives

46. In 2014, the average daily trading in exchange-traded derivatives increased 8% from the 2013 level. The average daily trading in futures products fell 3%. Among futures products, HSI futures and HSCEI futures were the most actively traded contracts, representing about 34% and 44% of all futures trading respectively. The average daily trading volume of HSI futures dropped by 14% compared to the 2013 level, whilst that of HSCEI futures rose 4%.

47. Average daily trading in options rose by 16% in 2014. Stock options remained the most actively traded options product and their trading volume rose 21%, compared to the 2013 level.



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

		2014	2013	2012
Futures	HSI Futures	69,098	80,247	82,905
	Mini-HSI Futures	28,177	32,188	34,810
	HSCEI Futures	89,005	85,538	64,863
	Mini-HSCEI Futures	13,884	9,232	6,356
	Stock Futures	1,731	1,882	1,315
	3-Month HIBOR Futures	0	0	1
	RMB Currency Futures ^	830	568	290
	Gold Futures	0	0	0
	Other futures products*	1,238	1,214	767
	Total Futures	203,965	210,869	191,176
Options	HSI Options	30,440	35,252	37,597
	Mini-HSI Options	3,892	4,743	5,014
	HSCEI Options	36,433	32,899	25,666
	Stock Options	301,797	249,295	228,438
	Other options products**	150	164	103
Total Options	372,712	322,353	296,818	
Total Futures and Options		576,676	533,222	487,994

Remarks:

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

^ RMB 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), FTSE/JSE Top40 Futures (launched on 30 Mar 2012), CES China 120 Index Futures (launched on 12 Aug 2013), London Aluminium Mini Futures (launched on 1 Dec 2014), London Zinc Mini Futures (launched on 1 Dec 2014), London Copper Mini Futures (launched on 1 Dec 2014).

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

Sources: HKEx and SFC Research

After-hours futures trading

48. The trading of HSI and HSCEI futures during the after-hours futures trading (AHFT) session relative to the daytime was more active in 2014 than in 2013. HKEx introduced mini-HSI futures and mini-HSCEI futures to its AHFT session on 6 January 2014. RMB currency futures were also included on 7 April 2014.
49. Moreover, to better match US market trading hours, the close of the AHFT session was extended from 11:00 pm to 11:45 pm, effective 3 November 2014.
 - In 2014, the average daily trading volume of HSI and HSCEI futures was 8,630 contracts, about 5.8% of the volume during the daytime session (6,636 contracts and 4.1% in 2013).
 - In 2014, the average daily volume of mini-HSI futures and mini- HSCEI futures was 3,264 contracts, about 8.3% of the volume during the daytime session.
 - In 2014, the average daily volume of RMB currency futures was 51 contracts, about 7.8% of the volume during the daytime session.