The times, they are changing. Over the past one and half months, we have gone through the most severe financial crisis that you and I have experienced. We have witnessed exceptionally volatile markets, and several regime-changing events. While policymakers around the world, including ourselves, continue to grapple with the implications of the on-going transformation of the global financial landscape and reflect on the lessons learnt and from there the makings of the new financial regulatory structure, let me share with you some observations and policy response from the Hong Kong perspective.

One can cite many factors contributing to this crisis:
- The recycling of the massive reserves accumulated by Asian sovereigns enabled the global economy to sustain very low real interest rates.
- Abundant liquidity in the global markets prompted an unrelenting search for yield, goaded by that mother of human frailties - greed.
- Asset price inflation supported the rapid expansion of mortgage credit and the loosening of credit standards over time.
- Asset securitisation, financial engineering, and the ever growing risk appetite combined to create credit risk transfer mechanisms which reduced risk transparency, fuelled excessive leverage, and built up massive maturity transformation risk in the global financial system.

Co-operation from the market
In the aftermath of the disappearance of top tier broker-dealers and the implementation of large scale government rescue packages worldwide, we are now going through an acute yet protracted de-leveraging process. Financial markets continue to go south. Market jitters have dramatically escalated. Investors increasingly seek reassurance from their governments that their investments are protected, that the institutions in which they have placed their investments and trust are good for their promise. The current crisis has threatened to unravel financial and banking systems, the arteries that supply life blood to the world’s finance and in turn the world economy.

In times of serious market dislocations, it is important that the regulator and the regulated work closely together. Over the last 18 months, we have been in close dialogue with many of you, asking for your view of the issues and trends in the market, whether you saw any part of our market fabric coming under pressure, whether fund managers had experienced inordinate redemptions, whether events in the other major markets were causing dislocations to the Hong Kong market, whether there was anything in the regulatory system that could be boned up to help manage the crisis, and many, many more questions. You were very helpful and patient with us, for which I must say thank you. Going forward, I hope we could continue
to count on your help, and for your frank and honest answers and discussions. It is crucial that we could, through each of you, access different information so that we could quickly put together a full picture. We need this picture to fashion a proper regulatory and policy response to the current crisis.

**Market participants should stay even more vigilant**

As the crisis tests the resilience of our financial institutions, it is important that each of you continue and increase your stress testing, examine your risk management models and functions, maintain adequate buffers and stay on top of the changing regulatory requirements around the world and make sure that you are in compliance. You will recall that I told you many times before that our doors are always open and you should come forward to discuss any issue that you feel require our focus. I reaffirm today that our doors will remain open.

**Cross-border regulatory co-operation**

Other than the co-operation of our regulatees, we also need to deepen and broaden the regulatory co-operation among regulators around the world. The world's financial markets are all inter-connected. Major operators like banks and hedge funds have global presence in these markets. It is not enough for the SFC to work on our own with our regulated community. Indeed, the recent crisis indicates clearly that the financial market tsunami has global reach, and demands global solutions.

Over the years, we have been building relationships with overseas regulators. We appreciate the long established relationship with the US SEC, and we look forward to further developing mutual co-operation with the SEC in cross-border regulation.

Let me give you some recent examples of our co-operation with the SEC. In 2006, we conducted joint inspections with the SEC on hedge fund managers licensed in both Hong Kong and the US, to review their infrastructure, corporate governance, risk controls, management of conflicts of interest, etc.

In 2007, the SEC conducted a seminar, namely “CCOOutreach”, at the SFC’s office targeting chief compliance officers of US-registered investment advisers located in Asia Pacific. The seminar covered various regulatory topics including risk assessment, portfolio management, brokerage arrangements, trade allocations, soft dollars, and performance advertising. It was well received by about 40 senior compliance personnel from the region. Most of them were based in Hong Kong and some came from Singapore and Sydney.

The collapse of Lehman Brothers last month, which reverberated around the world causing serious dislocations in all the major markets, underscores the need for global co-operation among the regulators around in the world. As news of the collapse of the talks to bail out Lehman Brothers emerged from the US and the world learned that Lehman Brothers Holdings Company was put under Chapter 11 of the US Bankruptcy Law, each of the markets had to grapple with fashioning its own solution to manage the crisis, including how to deal with the local Lehman subsidiaries each of whom could be facing different challenges and implications.

Markets have evolved so that financial institutions and participants operate across national borders, but regulation has remained confined within national borders. One of the inevitable results of globalisation is that there are no effective firewalls between markets. The crisis has
demanded a coordinated and consistent response by authorities around the world in order to restore market confidence and stability. The experience points to the need to review the regulatory framework and structure in a global context in order for regulation to be more effective in today’s financial landscape and global marketplace.

It is in the interest of all of us regulators to co-operate on multi levels, for instance, apart from the regulatory assistance we have provided one another on specific areas of our work such as licensing, fund authorisation, investigation and enforcement, we should also build platforms for exchange of information on specific intermediaries and macro, market issues.

The calls for all different jurisdictions to work together to build a new financial order and an appropriate supervisory architecture to go with it are gaining support around the world. Indeed, a meeting among the G20 will be held in Washington on 15 November 2008. While world leaders may not be able to start drilling into any detail at this meeting, their consensus on global co-operation in financial market supervision will be a major step forward.

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