Ladies and gentlemen, good afternoon. Thank you for inviting me here today to share a few thoughts with you.

It has been a while since I last stood before this forum in January last year. Since then, a series of market events has unfolded. While challenges continue to persist in the current economic environment, we must now look forward. Today, I would like to touch on a couple of matters which have ramifications for Hong Kong’s financial markets and which will contribute to shaping Hong Kong’s tomorrow as an international financial centre. The first of these is a regulatory development, namely the investor protection proposals that the Securities and Futures Commission has recently published for consultation. The second will impact the future development of Hong Kong’s financial markets, leveraging especially on our position of advantage to develop into China’s offshore RMB centre.

Let’s spend a few minutes on the current public consultations.

Consultation—general introductory remarks

As many of you will be aware, we have published a number of consultation papers recently. The largest, both in terms of scope and pages to read, is the consultation on proposals to enhance protection for the investing public. That paper addresses requirements for authorization of investment products and their offering documents, where they’re proposed to be offered to the retail public in Hong Kong, and also point-of-sale and other intermediary conduct requirements, as well as certain post-sale requirements. It introduces a brand new product code for unlisted structured products, and proposes changes to the existing codes on unit trusts and mutual funds and investment-linked assurance schemes and also to the code of conduct applicable to regulated intermediaries.

In the time since we published that paper at the end of September, we have been proactively seeking comments and feedback from stakeholders. As well, we have been holding briefing sessions and other more informal meetings to encourage constructive dialog about the various detailed proposals.

I will largely restrict my comments to the parts of the consultation paper that deal with requirements affecting issuers of investment products. Judging by the feedback we’ve had so far on these parts, two of the main areas of focus for the market in this area are the prospect of the imposition of a cooling-off period for purchases of investment products and the requirement for a user-friendly summary of key features and risks of investment products. I would like to take the opportunity to consider each of these items in a little more detail.
Consultation—cooling-off periods

First, let’s turn to cooling-off periods.

The consultation paper devotes a separate section to considering whether a cooling-off period should be implemented for some or all investment products.

At the outset, I should make the point that when we use the term “cooling-off”, it’s short-hand. In some circumstances, it could mean a period of time prior to execution of a trade in a particular investment product during which an investor could cancel a subscription or purchase order. In other circumstances, it could be a right on the part of the investor to require the issuer or distributor to buy back an investment product after the subscription or sale.

Obviously, this would have an effect at both the product issuer and the distributor level. If the feedback we receive from the consultation indicates support for cooling-off periods, provision would need to be made for implementation at both levels. I will focus my discussions today on the issuer level.

The implications for the issuer are several:

(a) Costs: We note in the paper that market value adjustments would need to be permitted in the case of some investment products, in addition to deductions for break funding costs associated with the exercise of cooling-off rights. There may also be administrative costs.

(b) Administrative burden: Issuers would need to ensure that their arrangements with distributors accommodated any such cooling-off rights and that adequate provision was made for processing of cancellations or buy-backs of investment products.

(c) Product design: Currently, some products are designed as “buy and hold” investments, some for quite lengthy terms. The need to provide investors with a right to exit within the first few days would impact upon product design and thus upon the variety of products available in the market.

There are two main implications for investors:

(a) Issuers may seek to build in the additional costs when pricing the product.

(b) Investors will in most cases not get back all of their principal when they exercise their cooling-off rights.

In our paper, we state our view that the imposition of a cooling-off period would offer greatest benefit to investors in the case of products with long lock-up periods and limited or no secondary markets or other liquidity.

Cooling-off periods already apply in the case of investment-linked assurance schemes. These are insurance policies where policyholders are making a long-term commitment, either with a single premium payment or regular premium payments, and where substantial surrender or withdrawal charges may apply should they need or wish to terminate or redeem.
the policy earlier than its scheduled maturity date. The question is, whether a cooling-off mechanism should be mandated for other investment products. In the case of products that should have a frequent or regular redemption facility, or where there is an active secondary market, or where market-making is provided on a regular basis, a cooling-off period may not offer as great a benefit to investors when weighed against the likely costs.

The main implication for distributors is the need to provide for refund of sales commissions, fees and charges paid by investors. Once again, we contemplate that there may need to be deductions for reasonable administrative costs on the part of the intermediaries in processing cancellations and buy-back requests.

We understand, however, that distributors have their concerns about the potential for abuse of cooling-off rights, for example, if the exercise of cooling-off rights becomes widespread and regular among retail investors, this would not only impose significant administrative burdens but also raise the question of whether distributors would be being fairly compensated for the time and effort they spend in fulfilling their obligations to clients. We are open to receiving your views on the matter.

Other, related issues that we’ve raised for public consideration include whether these rights should be made available to all investors or not. Some of the jurisdictions we have reviewed exclude certain transactions, for example situations where the investor has invested in the same product previously. We’re also conscious of the potential for investors to become less vigilant in reviewing products at or prior to the point-of-sale, and the danger that the right may be abused by those investors who take advantage of the ability to exit an investment to engage in short-term trading without having to be penalised for costs incurred. To discourage speculation, we propose that the amount payable in respect of a product upon exercise of a cooling-off right would need to be capped at the total principal amount invested.

We encourage interested parties to give us their detailed feedback on these matters.

**Consultation— Product Key Facts Statements**

Another of the main areas of stakeholder interest is the proposal for “Product Key Fact Statements” describing investment products in simple and brief terms.

One of the messages we have obtained from the market is that not all investors read product offering documents before making their investment decisions, because the documents are often too long and it is difficult to identify the important parts. Instead they rely on the much-briefer marketing materials. These materials, however, have the sole purpose of attracting investor attention to the products being featured and may not adequately convey the risks associated with the product.

In recent months, many different jurisdictions and supranational organisations have come out with their own versions of a summary document for one or more types of investment product. We have “Key Information Documents” or KIDs being proposed by the Committee of European Securities Regulators, “Product Highlights Sheets” proposed in Singapore, fund fact sheets in Malaysia and “Key Information Memoranda” in India, among others. The US SEC is working on a similar project with the industry.
The underlying common intent here is clear—to provide investors with clear, succinct and useful disclosure, in a user-friendly format, and to enable easier reading and comparison among investment products.

For our part, we prepared illustrative templates of Product Key Fact Statements for various types of investment products and provided these for consideration as part of the consultation. These templates are intended as guides. The basic requirement is that the document contains key features and risks of the particular product. In Hong Kong, the summary document will form part of the overall offering document for an investment product.

Our aim here is not to get bogged down in matters of form over substance. We support global efforts to harmonise standards and approaches to financial regulation. We recognize that many investment products are offered in many places at the same time, and that superficial differences between jurisdictions in their requirements for offering documents can contribute significantly to compliance costs and logistical difficulties for issuers and distributors. We have indicated, therefore, that we are open to comments and suggestions from issuers of these types of documents on any such difficulties they may face in practice and their suggestions on efficient ways to ensure that they satisfy substantive requirements in Hong Kong while accommodating the fact that other jurisdictions may have their own take on what these summary documents should look like.

The period during which we invite comments and feedback on the proposals has several weeks left to run, and we encourage all interested parties to avail themselves of the opportunity.

**Addressing Hong Kong’s future development as an IFC – role as the nation’s offshore RMB centre**

Sound regulation helps to provide the necessary framework for the market to progress and make its way forward. I’ve commented on some of the proposed regulatory enhancements, and I’d like to complement that perspective with a look at the broader picture and initiatives that help fortify Hong Kong’s role as an international financial centre. As I mentioned at the beginning, I would like to take some time to focus on the future development of Hong Kong as an offshore RMB centre for China – heralded by several successful RMB bond issuances to date.

**Hong Kong’s bond market—general remarks**

The financial secretary underscored the administration’s commitment to promoting growth in the debt market in this year’s budget speech. The Hong Kong government bond program is expected to contribute to the expansion of Hong Kong’s bond market, encouraging participation by foreign investors and domestic institutional investors. Another significant development is the recent sovereign RMB bond issuance in Hong Kong—the first outside the Mainland.

**Hong Kong’s role in the progress of the RMB**

In a speech I gave earlier this year, I said that the internationalization of the RMB would be a defining event of this century, and that I was confident that it would happen in our working
lifetime. In addition to the then-anticipated sovereign bond issuance, I also noted the plan to widen the scope of institutions and companies that may issue RMB bonds in Hong Kong.

China has indicated its intention to internationalise the RMB. Evolution of the RMB into an international currency will have major ramifications not only for China, but also for the global economic and financial landscape. Hong Kong is both part of China and the country’s offshore financial centre; it is thus naturally placed to support this pivotal transformation which we expect to see happen in the foreseeable future. In fact, we have already commenced “touching the stones while crossing the river” through the sovereign and corporate issuance of RMB bonds in Hong Kong.

**Hong Kong’s bond market—RMB-denominated bonds**

Hong Kong’s first RMB-denominated bond issuance was the RMB 5 billion issuance by the China Development Bank in 2007. Since then, several other policy or commercial banks have issued RMB-denominated bonds. To date, there have been 13 issues of RMB bonds in Hong Kong so far, from 8 different issuers, aggregating some RMB 38 billion.

Hong Kong has made much headway in this crucial area this year. The Ministry of Finance’s sovereign issuance of RMB 6 billion-worth of RMB bonds in September had symbolic significance in emphasising Hong Kong’s progress in becoming the offshore RMB centre for the nation.

While it is acknowledged the internationalisation of RMB is a transition that will not happen overnight, the sovereign bond issuance seems to be viewed by commentators as one of the first, small steps in the Mainland’s road towards reaching that ultimate goal. As you know, other measures include China’s currency swap agreements aggregating approximately 650 billion RMB with countries such as South Korea, Malaysia, Belarus, Indonesia and Argentina, as well as Hong Kong, and the pilot scheme permitting international trade settlement in RMB between several major trading cities1 and offshore centres being Hong Kong and Macau.

**Hong Kong’s role in the progress of the RMB**

Hong Kong is uniquely placed to become the premier RMB centre outside the Mainland, with increasing capacity to handle RMB-denominated financial transactions. With the benefit of the advances made this year, we will continue to work to grow Hong Kong’s RMB bond market and capture the opportunities presented to us.

Of course, not only is Hong Kong the natural choice to provide the services and infrastructure required to support these initiatives, we also see this as a bright prospect for Hong Kong’s own financial markets, thus a benefit both to the Mainland and to Hong Kong.

In building on progress so far and striving to reach the necessary critical mass, we need to continue to develop the use of the RMB in Hong Kong, along with augmenting infrastructure, permitting a wider range of investors to hold and trade in the currency, and expanding the universe of RMB-denominated instruments and financial transactions available to them. We

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1 Eligible enterprises in Shanghai, Guangzhou, Shenzhen, Zhuhai and Dongguan are permitted to settle in RMB with Hong Kong and Macau; eligible enterprises in Yunnan and Guangxi are permitted to settle in RMB with the 10 ASEAN countries.
have been working closely with the HKMA and with our Mainland counterparts towards expanding the range of issuers of RMB-denominated financial products and increased investor access to, and ability to invest in, RMB bonds, as well as development of other types of RMB-denominated investment products.

In addition to direct dialogue and specific programmes, Hong Kong enjoys a leading role in other policy initiatives such as the Plan for the Reform and Development of the Pearl River Delta. This Plan was outlined by the National Development and Reform Commission in January 2009, and reflects the strategic position taken by China on development of the Pearl River Delta region. It provides us with a facilitative platform to run “pilot measures” and experiment with new ideas and new products. The Plan contemplates, among other things, the establishment of trial programmes to accommodate financial innovation and facilitate the flow of financial business between the two regions. In particular, our participation in the Hong Kong – Guangdong Financial Expert Group allows us the opportunity to make further definitive progress in implementing the Plan. There may be scope for exploring further use of Hong Kong’s RMB capabilities and participation in its debt capital markets by Guangdong enterprises, which would in turn contribute towards efforts to increase use and circulation of the RMB.

To date, investment in RMB bonds in Hong Kong has mainly been retail-based and there is little secondary market trading in the bonds. As the pace of RMB bond issuances gathers accelerating momentum, China continues to press ahead with its plans for the RMB and Hong Kong continues to develop its capabilities and capacity to accommodate RMB-denominated services and products, institutional involvement in the RMB bond market and markets for other RMB products will be a necessary and inevitable part of the equation.

In the wider context, Hong Kong must continue its efforts to grow its debt markets and enable wider participation including institutional participation. The potential for growth in RMB-denominated financial products in particular is enormous, and Hong Kong is well-placed both to support these developments and to benefit from them.

We look forward to working with you towards our common objectives of growth and increased opportunities for Hong Kong’s financial markets.

Thank you.