Good morning ladies and gentlemen

I would like to first thank the Hong Kong Investment Funds Association for inviting me here today. I look forward to sharing with you recent significant developments in the fund industry, a focused stock take of Hong Kong's position as an international asset management centre and some thoughts on how to maintain forward momentum in a manner that benefits the entire fund industry in Hong Kong.

RMB business in Hong Kong

I would first like to talk to you about RMB business in Hong Kong. The RMB story is an ongoing success story that we can all be proud of.

It was in 2009 when the Mainland launched the pilot cross border RMB trade settlement scheme, when I first floated the idea of how the wider international use of RMB would be a game changer for the Hong Kong financial industry. A lot has happened since.

The Bank for International Settlements has published the Triennial Central Bank Survey of turnover in foreign exchange markets (2013). The report shows that the RMB has become the ninth most traded currency in the world, ahead of the Hong Kong dollar. In the last survey (in 2010), RMB was a far distant 17th. I believe it is only a matter of time before the RMB will occupy a place at the very top of the global currency league. In fact, data that SWIFT released yesterday shows, RMB has already surpassed the Euro to take second place as the most widely used currency in global trade finance.

Let's examine the numbers. In terms of SFC-authorized funds alone, RMB funds have grown from literally nothing three years ago into a sizeable product category with about RMB70 billion under management. By introducing one new product into the market after another, you have helped Hong Kong open up a significant lead.

Success also attracts talent, like bees to honey. More international fund managers are coming to Hong Kong to add to the diversity and depth of our talent pool. This is one of Hong Kong’s strengths; and it underscores the value and attractiveness of our open markets. I will talk more about this later.

What is less clear is how the rise of the RMB would affect the global financial industry and Hong Kong's place in it. So far, Hong Kong is ahead in the game. We are the undisputed leader in offshore RMB business. There are a number of reasons for this. External factors
have played their part but other factors are rooted much closer to home. Let me explain what I mean.

It takes two hands to clap; we must acknowledge the favourable Mainland policies. For example, the RQFII initiative that Mainland authorities launched in December 2011 was groundbreaking. It allows the investment of offshore RMB into the Mainland securities markets. Mainland authorities have since expanded the initiative repeatedly, in terms of eligible applicants, size and investment scope.

Due to this, more firms are now able to participate in the scheme, launching funds that employ more diverse strategies. This adds to Hong Kong’s RMB product offerings, putting us further ahead in the game. For that, we must thank Director-General Xu Hao and his colleagues at China Securities Regulatory Commission and other Mainland authorities.

Of course, I should also applaud you all for turning policy initiatives into business opportunities. And I note that among you are international asset managers who recently joined us here in Hong Kong eager to capture a slice of the business.

The pillars behind Hong Kong’s success

The success of RMB business and the prospect of the Mainland opening its markets further is, without doubt, exciting for everyone. The whole world is watching.

Yet amid all the excitement about RMB products and Mainland-related business, it is also important for Hong Kong that we continue to maintain and expand our open markets.

Of course, RMB and Mainland-related funds are an important part of our fund industry. They are fast-growing and dynamic but the Hong Kong story is larger than this.

One of the reasons why we have established Hong Kong as a leading international asset management centre in just three decades is because we maintain an open market. This approach is underpinned by our belief that it should be the market, rather than the regulator, that determines the success of a product or a firm. There are also good strategic reasons for us to adopt an open approach. When we first started developing our asset management industry in the 1980s, our market was very small. The quickest way to gain critical mass was to bring in outside players, and their products.

Today, this philosophy still holds. Out of 1800 SFC authorized funds, only about 300 are Hong Kong domiciled. This just shows how open our market is to overseas products and firms.

We embrace all who are willing to come and use the Hong Kong platform. Of course, we expect them to have experience, talent, integrity and the conduct required under our rules and regulations. If they meet those requirements, it does not matter where they come from, what their background is or who their parent companies are. We have a transparent set of standards to protect investors and maintain market integrity. As long as you meet them, we welcome you with open arms.

The combination of an open market and embrace our willingness to all manner of worthy professional talent is a heady cocktail that has worked out spectacularly for Hong Kong’s fund industry. The record high AUM of HKD12.6 trillion of our combined fund management
business at end 2012 ranks us among the top asset management hubs in Asia. Australia was ahead of us by only a very slim margin.

Our open market and sound regulatory framework attracts money from investors globally. Over 60% of our assets under management come from overseas investors.

**How the Mainland story fits into our open market approach**

Of course, RMB and the Mainland are very important to us too. It is, after all, one of the key reasons why international fund managers and investors come to Hong Kong.

So how can we build on our traditional core strengths and meld the vital Mainland factor into a powerful engine for growth that will keep firms, talent and capital flowing into Hong Kong?

**Enhancing the Hong Kong platform**

This question brings me to my next topic on enhancing the Hong Kong platform.

Hong Kong’s strength traditionally has been fund distribution and sales. About three quarters of the industry’s staff work in this area. Successful fund distribution requires creativity, being in sync with the market and no small amount of street smarts to assess investor needs, and create demand for products. This is certainly an area of strength for Hong Kong.

For the longer term, though, I believe that we need to add new dimensions to our industry. Investment portfolio management is one potential area. Fund administration, such as domicile, custodian and administrative services, is another. I am talking about a vision and roadmap to create a seamless end-to-end asset management platform.

Such a platform is made possible by 2 factors. The first is the opening up of the Mainland capital market to international investors and Hong Kong’s role as the gateway to the Mainland. In carrying out this role, we have accumulated a deep pool of knowledge about the Mainland market. When international investors look for a base for their Mainland-focused operations, naturally, they choose Hong Kong.

From this baseline, we are gradually building up our expertise in investment portfolio management. Over the past few years, the number of Hong Kong-domiciled funds has been increasing by an average of around 30% a year.

The second factor is the export of capital by the Mainland and its investors, looking for investment and risk diversification. As the Mainland’s economy continues to bring wealth to its citizens, they increasingly see the need to grow that wealth. Like all investors around the world, they will want the option of investing through professional managers in markets around the world. Already we have begun to see Mainland investors availing themselves of the services of Hong Kong-based investment managers. A significant portion of QDII products on the Mainland, for instance, are products advised by Hong Kong-based managers.

As you all know, we are working on a mutual recognition of funds between Hong Kong and the Mainland. This initiative will allow Hong Kong managers to sell their funds in the Mainland and Mainland managers to sell their funds in Hong Kong. This will, in turn, provide those Mainland investors wanting to invest in overseas markets easy access to those markets through our Hong Kong funds. Once implemented, this program will give fund managers greater incentive to set up in Hong Kong, thus adding to what Hong Kong has to offer.
As well, when Mainland funds come to Hong Kong on the mutual platform, this will immediately open our RMB investment products market further by providing much broader spectrum and depth. That will, in turn, promote a healthy cross fertilization of asset management skills here, adding to the vibrancy and richness of our talent pool.

Meanwhile, we are also working on improving Hong Kong's infrastructure to support an end-to-end value chain. We are working with the Government on the introduction of an open-ended fund company structure for Hong Kong. The proposed open-ended fund company structure will allow fund managers to set up investment funds in Hong Kong in the form of a corporation with variable capital, giving them more flexibility in structuring their funds.

This new legal structure will be offered to the industry in addition to the existing unit trust structure. This should provide market participants with more choice and greater efficiency in establishing and operating Hong Kong domiciled funds.

**Summing up**

Over the past few years, Hong Kong's asset management industry has experienced tremendous growth. We have more firms, more products, and more assets under management. Growth has been very good but just as important is the need to take positive steps to move up the value curve by broadening and deepening our knowledge and improving our infrastructure. It is clear from the decisions made in the Third Plenary Meeting, that the Mainland will push through market reforms with renewed focus, energy and force. With that, new opportunities will continue to emerge from the Mainland. We need to ensure that our platform is robust and attractive enough and there is sufficient expertise here for us to capture those opportunities.

In parallel, we need to maintain our open market approach and continue to welcome and attract overseas funds and expertise.

And now ladies and gentlemen, I know that you are all eager to learn more about the mutual recognition program. So let me share with you all an update on the Mutual Recognition of Funds Initiative to conclude my speech here today.

Back in January this year, we unveiled the fact that we, together with our Mainland counterparts, formed a working group to study the proposed mutual recognition of funds between Mainland and Hong Kong. After a year of hard work, today I am pleased to be able to tell you that we are in the final stretch of this project. My team is working hard to settle the final details. We are making good progress. Once we are done, we will issue an official announcement on the detailed arrangements.

Director General Xu Hao has just unveiled for you some of the key rules of engagement that will underpin the mutual recognition program. Let me now share with you the 3 principles that have guided the design of this initiative.

First, the Mutual Recognition of Funds Initiative is premised on the principles of mutuality and respect. For this initiative to work, we must respect the rules and regulations of our respective jurisdictions. The two regulators will agree common rules and standards. Each side will respect the rules of the other, and neither side should expect any preferential treatment.
Second, this initiative must be a win-win situation for both parties. Here’s how I see it: Mainland fund managers and fund products will have unfettered access to international markets and investors through the Hong Kong platform. It is a golden opportunity for them to participate in global markets. For Hong Kong, this initiative will reinforce our position as a major international fund management centre. This is a first-in-the-world opportunity for any outside fund manager to directly sell its fund products in the Mainland. To enjoy this privilege, outside fund managers must be licensed by the SFC and their funds domiciled in Hong Kong.

Thirdly, this is an initiative of great significance for both Hong Kong and the Mainland. It cannot and should not be rushed. We need to take a measured, pragmatic and possibly more conservative approach to facilitate a successful roll out. With this in mind, we will start with regular and plain vanilla type products. We will, of course, consider allowing greater diversity at a later stage, once the initiative is successfully underway and running smoothly.

Thank you and I wish you all a successful conference.