

For Information

Legislative Council Panel on Financial Affairs

- (A) Progress report on the proposed Issuance of Government Bonds
and
(B) Summary outcome of the Securitisation of Future Revenue
from Government tolled tunnels and bridges**

(A) Progress Report on the proposed Issuance of Government Bonds

In response to sub-paragraph 3(b) of the minutes of meeting of the LegCo Subcommittee on Proposed Resolution under section 3(1) of the Loans Ordinance (by way of issue of Government bonds) held on 13 May 2004, the Administration would like to provide the following information regarding the proposed offering of Government bonds for the Panel's reference.

2. On 28 May 2004, Government announced that following a competitive selection exercise, the BOC Group (consisting of BOC International Holdings Limited and Bank of China (Hong Kong) Limited) and Merrill Lynch were jointly selected as the Arrangers and Joint Global Coordinators for the proposed offering of Government bonds of HK\$ 20 billion (the Offering). In discharging their responsibility in recommending a suitable syndicate for the Offering, BOC Group and Merrill Lynch recommended that HSBC also be appointed as Arranger and Joint Global Coordinator for the Offering.

3. Since the above announcement, the three firms have worked closely with the Government to prepare for the Offering, including recommending to the Government the following firms to be appointed as Joint Lead Managers and Bookrunners of the three parts of the Offering :-

For the HK\$ Retail offering :	BOC Group, HSBC and Standard Chartered Bank
For the HK\$ Institutional offering :	BOCI, Citigroup, HSBC and Merrill Lynch
For the US\$ International offering :	BOCI, Goldman Sachs, HSBC, Merrill Lynch and Morgan Stanley

Government has accepted these recommendations.

4. Preparatory work in connection with the structuring of the bonds, drafting of legal documentation and due diligence have now been completed. A copy of the formal announcement dated 7 July 2004 is at **Enclosure 1**. As there are stringent regulatory restrictions in either the local or overseas capital markets relating to any publicity prior to the Offering, the Government is not able to disclose or discuss further details relating to the Offering at this stage.

(B) Securitisation of Future Revenue from Government tolled tunnels and bridges

5. In response to sub-paragraph 3(c) of the minutes of meeting of the LegCo Subcommittee on Proposed Resolution under section 3(1) of the Loans Ordinance held on 16 January 2004, the paragraphs below summarise the overall outcome of the securitisation exercise (the HK Link 2004 transaction).

6. The HK Link 2004 transaction marked the first ever securitisation bond offering by the Government. It is also the first securitisation bond offering to retail investors in Hong Kong. It is the first securitisation bond to be listed on the Hong Kong Stock Exchange (HKSE) and the first simultaneous offer of bonds to both retail and institutional investors by any single issuer in Hong Kong.

7. Over 800 branches of 23 placing banks were involved in the retail offering, along with 89 brokers who participated via the Central Clearing and Settlement System of the HKSE. The retail offering received a total of 35 403 valid applications for a total of \$7,577.5 million worth of bonds. Given the total size of retail bonds on offer at \$2,470 million, the bonds were over two times oversubscribed. On the institutional tranches, the total size of orders received were \$14.48 billion while the total size of institutional notes on offer was \$3.53 billion. The notes were over three times oversubscribed.

8. The key terms and conditions of the retail bonds offered are summarised in the extract of the Prospectus at **Enclosure 2** for members' ease of reference.

Treasury Branch
Financial Services and the Treasury Bureau
July 2004

7 July 2004

**HONG KONG SPECIAL ADMINISTRATIVE REGION
GOVERNMENT GROUND-BREAKING INAUGURAL
RETAIL BONDS**

The Government of the Hong Kong Special Administrative Region (“HKSAR Government”) has today launched its inaugural retail bond offering (“Retail Bond Offering”) comprising two Hong Kong dollar (HKD) retail tranches.

The Retail Bond Offering, which opens tomorrow at 9:00 am, is part of an inaugural global bond offering of up to HK\$20 billion (“Global Bond Offering”). The Global Bond Offering comprises:

- A US dollar-denominated, Rule 144A / Regulation S institutional tranche of 10-year notes
- Two HK dollar-denominated, Regulation S institutional tranches of 5-year notes and 15-year notes
- Two HK dollar-denominated retail tranches of 2-year bonds and 4-year bonds to be offered to Hong Kong retail investors

The subscription period for the retail tranches closes at 2:00 pm 16 July 2004.

Speaking at the Retail Bond Offering launch ceremony, the Financial Secretary of the Hong Kong Special Administrative Region, The Honourable Henry Tang, said: “This is a ground-breaking transaction, and one that gives retail investors an opportunity to invest for the future of Hong Kong. With the Government bonds offered to both retail investors and institutional investors, this offering will help further extend the capabilities of our local capital market and reinforce the prominent position of Hong Kong as an international financial centre.”

The yield for the Retail Bonds will be fixed and benchmarked to Exchange Fund Notes rates. A semi-annual coupon will be paid to investors starting after the first six months.

Retail Offering	Tranche A	Tranche B
Tenor	2 years	4 years
Minimum Issue Amount	HK\$50 million	HK\$50 million
Currency	HKD	HKD
Coupon (p.a.)	2.13%	3.38%
Minimum Denomination	HK\$50,000	HK\$50,000
HKSAR Government Credit Ratings (S&P/Moody’s/Fitch)	AA-/Aa3/AA+	AA-/Aa3/AA+

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HKSAR Government retail bond offering launch/2

The BOC Group (consisting of Bank of China (Hong Kong) Limited and BOCI Asia Limited), HSBC and Merrill Lynch are the Arrangers and Joint Global Co-ordinators (JGCs) for the HK\$20 billion Government bonds. The Joint Bookrunners for the Hong Kong Retail Bond Offering are:

- BOC Group (Bank of China (Hong Kong) and BOCI Asia Limited)
- HSBC
- Standard Chartered Bank (HK) Ltd.

Mr Gary He Guangbei, Vice Chairman and Chief Executive of Bank of China (Hong Kong), said: “We are honoured to be one of the arrangers and Joint Global Coordinators working with the HKSAR Government. This inaugural bond offering will provide an alternative source of capital for the Government to invest in infrastructure and investment projects that will bring long-term economic benefits to Hong Kong, and facilitate further development of the local bond markets.”

The Hongkong and Shanghai Banking Corporation Limited Chairman Mr David Eldon said: “We are honoured and proud to be associated with this ground-breaking transaction. This represents Hong Kong’s coming of age in the debt capital markets. There are many important new features associated with this transaction. I think key amongst them is the level of retail participation that is being offered to Hong Kong people to invest in Hong Kong’s future.”

Mr Tan Kong Khoon, Head of Consumer Banking of Standard Chartered Bank (HK) Ltd, said: “The retail bond issue from the HKSAR Government is another milestone in the development of the bond market in Hong Kong, and we are honoured to be one of the Joint Bookrunners for this very important transaction.”

Similar to the HK\$6 billion securitisation bonds launched by the HKSAR Government earlier in the year, the Retail Bond Offering will also be offered to Hong Kong retail investors through a large number of placing banks and retail brokers. The HKSAR Government’s bonds will also be listed on the Hong Kong Stock Exchange.

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HKSAR Government retail bond offering launch/3

The net proceeds of the HKSAR Government bonds will be credited to the HKSAR Government's Capital Works Reserve Fund to provide an alternative source of funding for infrastructure and other investment projects.

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Issued by The Hongkong and Shanghai Banking Corporation Limited on behalf of BOC Group (Bank of China (Hong Kong) and BOCI Asia Limited), The Hongkong and Shanghai Banking Corporation Limited and Standard Chartered Bank (HK) Ltd. as the Joint Bookrunners for and on behalf of the Hong Kong Special Administrative Region Government.

The information contained herein does not constitute an offer to sell or the solicitation of an offer to buy the securities of HKSAR Government in the United States. HKSAR Government's securities may not be offered or sold in the United States absent registration under the United States Securities Act of 1933 or an exemption from registration. Any public offering of securities in the United States will be made by means of an offering circular that can be obtained from the HKSAR Government, and the offering circular will contain detailed information about the HKSAR Government. No money, securities or other consideration is being solicited by this document.

The information contained herein also does not constitute an offer to sell or a solicitation of an offer to buy HKSAR Government's securities nor shall there be any sale of such securities in any state or country in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such state or country.

SUMMARY OF THE RETAIL BONDS BEING OFFERED

The information set out in this section is subject to, qualified by, and must be read in conjunction with, the further detailed information under the section headed "Transaction Summary", in this Prospectus and in the Transaction Documents. Capitalised terms used, but not defined, in this section shall have the meanings ascribed to it under the section headed "Transaction Summary". The terms and conditions of the Retail Bonds are issued in the English language and the English version will prevail over the Chinese language version in the event of conflict or discrepancy.

THE RETAIL BONDS

Tranches of Retail Bonds

Tranche A Retail Bonds
Tranche B Retail Bonds
Tranche C Retail Bonds

Use of Proceeds and payment of issuance expenses

The Issuer will use the gross proceeds of the Retail Bonds and the Notes up to a maximum of HK\$6,000,000,000 to subscribe for the Toll Revenue Bond on or about the Issue Date. HKSAR Government will authorise the Issuer to pay certain fees and expenses payable by HKSAR Government in connection with the transactions set out in this Prospectus on behalf of HKSAR Government by making such payments in partial discharge of the Issuer's obligation to pay the subscription amount of the Toll Revenue Bond to HKSAR Government.

Subscription Period

9:00 am on 20 April 2004 (Tuesday) to 2:00 p.m. on 29 April 2004 (Thursday) (the "**Subscription Period**").

Price-fixing Date

4 May 2004 (Tuesday) (the "**Price-fixing Date**").

Issue Date

7 May 2004 (Friday) (the "**Issue Date**").

Application for Retail Bonds

Application for Retail Bonds will only be made by the Placing Banks or HKSCC (either directly if you are a CCASS Investor Participant or through your designated CCASS Broker/Custodian Participant).

In order to instruct a Placing Bank to apply for Retail Bonds on your behalf, you must already have, or you must open, a bank account and also an investment account with the Placing Bank you intend to instruct. In order to instruct HKSCC to apply for Retail Bonds on your behalf, you must already have, or you must open, an Investor Account with HKSCC, or apply through your designated CCASS Broker/Custodian Participant who is willing to make the application on your behalf. See the section headed "How to Apply for the Retail Bonds".

Each of HKSCC, your designated CCASS Broker/Custodian Participants and Placing Banks have different arrangements for accepting and processing application instructions, for example, there are differences in their operating hours during which application instructions will be accepted, their requirements as to when Application Amounts will be debited, the amounts of charges imposed by them and the arrangements for making refunds (if any) to you. **You should familiarise yourself with, and ensure you understand and accept, the terms and conditions of HKSCC, the Placing Bank or your designated CCASS Broker/Custodian Participant, as the case may be, before you instruct it. See the section headed “How to Apply for the Retail Bonds”.**

Application Price

The application price of each tranche is 102 per cent. of the principal amount of the Retail Bonds (the “**Application Price**”). The Application Price has been set at a level which is intended to facilitate subscription and allotment logistics and is not intended to reflect any expectation as to the Subscription Price of the Retail Bonds of any tranche.

The Subscription Price of each tranche of Retail Bonds may be equal to or less than the Application Price for that tranche of Retail Bonds.

Subscription Price

The subscription price of each tranche (the “**Subscription Price**”) will be expressed as a percentage of the principal amount of the Retail Bonds and it will be the lower of:

- (a) the Application Price, being 102 per cent. of the principal amount of the Retail Bonds; and
- (b) the percentage determined on the Price-fixing Date so that the Retail Bonds of that tranche will have an annualised yield equal to the annualised yield of an identified issue of Exchange Fund Notes (“**EFN**”) of comparable remaining tenor, plus a specified margin, as follows:

Annualised Yield of Tranche A Retail Bonds =
EFN 5706 yield + 0.45 per cent.

Annualised Yield of Tranche B Retail Bonds =
EFN 5903 yield + 0.60 per cent.

Annualised Yield of Tranche C Retail Bonds =
EFN 7102 yield + 0.75 per cent.

where the determination will be made on the Price-fixing Date by reference to the fixing page of the HKMA in 0#HKEFBN=MIDF at or about 11:30 a.m. If the annualised yield of an identified issue of EFN is not available, the Reference Agent and the Trustee jointly shall have the discretion to select another issue of EFN of comparable remaining tenor for price-fixing purposes.

The Subscription Price may be equal to or less than the Application Price.

Handling Fee and Brokerage Fee

The Placing Bank to which an applicant for the Retail Bonds gives his instructions will charge a handling fee of 0.15 per cent. of the Subscription Price of Retail Bonds which are allotted to the applicant (the "**Handling Fee**").

HKSCC or your designated CCASS Broker/Custodian Participants, as the case may be, to which an applicant for Retail Bonds gives his instructions will charge a brokerage fee of 0.15 per cent. of the Subscription Price of Retail Bonds which are allotted to the applicant (the "**Brokerage Fee**").

Each applicant will be responsible for the payment of the Handling Fee or the Brokerage Fee.

Application Amount

Upon application for the Retail Bonds:

- (a) where the applicant applies for the Retail Bonds through a Placing Bank, the applicant is required to pay an amount equal to the Application Price, plus a handling fee of 0.15 per cent. of the Application Price of the Retail Bonds the applicant applies for (the "**PB Application Amount**"); and
- (b) where the applicant applies for the Retail Bonds through HKSCC, the applicant is required to pay an amount equal to the Application Price, plus a brokerage fee of 0.15 per cent. of the Application Price of the Retail Bonds the applicant applies for (the "**CCASS Application Amount**").

(together, the "**Application Amounts**" and each an "**Application Amount**").

Subscription Amount

The actual amount the applicant is required to pay for the Retail Bonds allotted to the applicant is equal to the Subscription Price of the relevant tranche of Retail Bonds plus the Handling Fee (the "**PB Subscription Amount**") or, as the case may be, the Brokerage Fee (the "**CCASS Subscription Amount**") (together, the "**Subscription Amounts**" and each a "**Subscription Amount**"). The Subscription Amount may be equal to or less than the Application Amount. If the Subscription Amount is less than the Application Amount, the difference will be refunded to the applicant.

Aggregate Principal Amount of Issue

The minimum issue amount of each of the Tranche A Retail Bonds, the Tranche B Retail Bonds and the Tranche C Retail Bonds is HK\$50,000,000 (the “**Minimum Issue Amount**”). The maximum aggregate principal amount of Retail Bonds and Notes is HK\$6,000,000,000; however, the Issuer reserves the right to fix the principal amount of Retail Bonds of each tranche to be issued in the light of valid applications received. If the principal amount of Retail Bonds of a tranche to be issued is less than the principal amount of Retail Bonds of that tranche which has been validly applied for, Retail Bonds will be allocated as described in the section headed “Allocation of Retail Bonds”.

None of the tranches of the Retail Bonds will be underwritten by any party and if the public subscription in relation to any tranche falls short of the Minimum Issue Amount, the Issuer will not issue the undersubscribed tranche and affected prospective investors will be refunded their Application Amounts in accordance with the section headed “How to Apply for the Retail Bonds”.

Allocation of Retail Bonds

If valid applications are received for a greater principal amount of Retail Bonds of any tranche than is to be issued, a minimum of HK\$50,000 in principal amount of that tranche will be allocated to each of the applications (the “**Applications**”) through (a) HKSCC from CCASS Investor Participants, and CCASS Broker/Custodian Participants (and so that if more than one valid application instruction is given from a prospective investor to its designated CCASS Broker/Custodian Participant, all such valid applications may be aggregated) and (b) the Placing Bank’s accounts through which valid application instructions were given (and so that if more than one valid application instruction is given from the same Placing Bank’s account, all such valid application instructions will be aggregated) and the Applications to receive the allocation will be chosen by ballot if valid application instructions for Retail Bonds of a tranche are received through HKSCC from CCASS Investor Participants and CCASS Broker/Custodian Participants and the Placing Bank’s accounts in a greater number than the number of Retail Bonds of that tranche to be allocated. The remaining Retail Bonds of that tranche will be allocated to each of the Applications on a pro rata basis to the remaining number of Retail Bonds validly applied for through each of HKSCC from CCASS Investor Participants or CCASS Broker/Custodian Participant or such Placing Bank’s account (rounded down to the nearest whole Retail Bond) and in the case of Retail Bonds remaining after rounding, by ballot. Fractions of Retail Bonds will not be allotted. No one will be allotted more Retail Bonds than they applied for.

Retail Bond Maturity Date

Bond Payment Date falling on or nearest to 7 May 2007 in respect of Tranche A Retail Bonds (the “**Tranche A Retail Bond Maturity Date**”);

Bond Payment Date falling on or nearest to 7 May 2009 in respect of Tranche B Retail Bonds (the “**Tranche B Retail Bond Maturity Date**”); and

Bond Payment Date falling on or nearest to 7 May 2011 in respect of Tranche C Retail Bonds (the “**Tranche C Retail Bond Maturity Date**”).

Redemption Price	100 per cent. of the principal amount of the Retail Bonds
Interest Rate	2.75 per cent. per annum in respect of Tranche A Retail Bonds 3.60 per cent. per annum in respect of Tranche B Retail Bonds 4.28 per cent. per annum in respect of Tranche C Retail Bonds
	Interest will be calculated and paid at the specified rates by reference to 100 per cent. of the principal amount of the Retail Bonds. The total return on the Retail Bonds, or yield to maturity, however, will depend on the Subscription Price. If the Subscription Price is greater than 100 per cent. of the principal amount of the Retail Bonds, the annualised yield will be lower than the specified interest rate (on an annualised basis); if the Subscription Price is lower than 100 per cent. of the principal amount of the Retail Bonds, the annualised yield will be greater than the specified interest rate (on an annualised basis). The Subscription Price will be expressed as a percentage of the principal amount of the Retail Bonds and will be fixed so that it will be the lower of (a) the Application Price and (b) the percentage so that the annualised yield on the Retail Bonds for each tranche is equal to the annualised yield of an identified issue of EFN of comparable remaining tenor plus a specified margin. See “—Subscription Price” above.
Frequency of Interest Payments	Interest payments will be made quarterly on each Bond Payment Date.
Payments on the Retail Bonds	All payments of principal and interest on the Retail Bonds will be made by credit to the designated bank accounts of the relevant CCASS Investor Participants or CCASS Broker/Custodian Participants or through the investment account in which the Retail Bonds are held. See the sections headed “Custody Arrangements in respect of the Retail Bonds” and “Settlement, Clearance and Custody”.
Denomination	HK\$50,000 per Retail Bond

Form of Retail Bonds

Retail Bonds in definitive form (“**Definitive Retail Bonds**”) will only be issued in limited circumstances. Three permanent global Retail Bonds (the “**Global Retail Bonds**”) in bearer form, each representing the total principal amount of a tranche of Retail Bonds, will instead be deposited on the Issue Date of the Retail Bonds with CMU operated by the HKMA. **Individual Retail Bondholders who apply for Retail Bonds by instructing a Placing Bank:**

- (a) **must initially hold their Retail Bonds in an investment account with a participant in the CMU; and**
- (b) **for the purpose of initial allotment of Retail Bonds, the Retail Bondholder must already have, or must open, a bank account and also an investment account with the Placing Bank to which he gives his application instructions.**

Individual Retail Bondholders who apply for Retail Bonds by giving electronic instructions to HKSCC (either directly as a CCASS Investor Participant or indirectly through their designated CCASS Broker/Custodian Participant):

- (i) **must initially hold their interests in the Retail Bonds allotted to them through an account with HKSCC (either directly as CCASS Investor Participant or indirectly through their designated CCASS Broker/Custodian Participant). HKSCC will in turn hold the corresponding interest in the Global Retail Bonds through its account with the CMU Operator; and**
- (ii) **for the purposes of the initial allotment of Retail Bonds, the Retail Bondholder must already have, or must open, an Investor Account with HKSCC, or a securities or custodian account with a CCASS Broker/Custodian Participant who is willing to make the application on its behalf.**

See the section headed “Custody Arrangements in respect of the Retail Bonds”.

The Retail Bondholder’s ability to pledge his interest in the Retail Bonds to persons who are not participants of the CMU, or otherwise to take action in respect of his interest, may be affected by the lack of definitive Retail Bonds.

Taxation

All payments of principal and/or interest in respect of the Retail Bonds will be made subject to withholding or deduction for or on account of any present or future tax, duty or charge of whatsoever nature imposed or levied by or on behalf of Hong Kong or any other authority having power to levy tax in Hong Kong. No such withholding or deduction is currently required. See the section headed “Taxation of Retail Bonds”.

No HKSAR Government Guarantee

The obligations of the Issuer to pay interest on each tranche of the Retail Bonds and to repay the principal amount of each tranche of the Retail Bonds when they mature are not guaranteed by, and are not obligations of, HKSAR Government. For other considerations relating to an investment in the Retail Bonds, see the section headed “Risk Factors”.

Listing

The Retail Bonds will be listed on the Hong Kong Stock Exchange. See the section headed “Trading of Retail Bonds on the Hong Kong Stock Exchange”. The listing of the Retail Bonds on the Hong Kong Stock Exchange does not assure liquidity or an active trading market for the Retail Bonds.

Market Making

Market makers have been appointed by the Issuer for each tranche of Retail Bonds and each market maker has, subject to certain limitations, agreed to quote prices at which it will buy or sell Retail Bonds in over-the-counter transactions. See the section headed “Market Making Arrangements”. These arrangements do not assure an active trading market for the Retail Bonds.

Cancellation of Retail Offering

The Issuer reserves the right to cancel the offering of one or more tranches of the Retail Bonds on or before the Issue Date for the Retail Bonds, in which case, no Retail Bonds of the relevant tranche or tranches will be issued and all applicants of the relevant tranche or tranches will be refunded their Application Amounts. The Issuer will give prompt public notice of such cancellation.

Security Interest in the Retail Bonds in favour of Placing Banks, HKSCC and CCASS Broker/Custodian Participants

The standard terms and conditions of the investment account, Investor Account or securities account or for the provision of custody services of each of the Placing Banks, HKSCC and the relevant CCASS Broker/Custodian Participants, as the case may be may permit it to take a security interest in, or to impose other restrictions on, the Retail Bonds credited to such account or to exercise a lien, right of set-off or similar claim against a Retail Bondholder in respect of monies held in any of his accounts maintained with such Placing Bank, HKSCC or CCASS Broker/Custodian Participant to secure any amounts which may be owing by the Retail Bondholder to such Placing Bank, HKSCC or the relevant CCASS Broker/Custodian Participant, as the case may be. In particular, if the Placing Bank, HKSCC or the relevant CCASS Broker/Custodian Participant, as the case may be, makes an advance to the Retail Bondholder in connection with the payment of any unpaid Subscription Amount of the Retail Bonds, the Placing Bank, HKSCC or the relevant CCASS Broker/Custodian Participant, as the case may be, may have the legal right to restrict the Retail Bondholder's ability to transfer the Retail Bonds, to collect amounts owing to it out of payments of interest or principal received on the Retail Bonds or to sell the Retail Bonds and recoup amounts owing to it or other sale expenses, duties and interest costs out of the proceeds of sale or to charge interest on amounts owing to it.

It is important that the Retail Bondholder should familiarise himself with, and ensure he understands and accepts the terms and conditions of operation of the investment account, Investor Account or securities or custodian account before making an application to open such account. See the section headed "Custody Arrangements in respect of the Retail Bonds".

Risk Factors

Prospective purchasers of the Retail Bonds should read and consider carefully the issues discussed in the section headed "Risk Factors".

Other Provisions

See the section headed "Transaction Summary — The Retail Bonds and the Notes — Common Provisions of the Retail Bonds and the Notes".