

立法會
Legislative Council

LC Paper No. CB(1)2937/10-11
(These minutes have been seen
by the Administration)

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Panel on Financial Affairs

Minutes of meeting
held on Thursday, 9 June 2011 at 2:30 pm
in the Chamber of the Legislative Council Building

Members present : Hon CHAN Kam-lam, SBS, JP (Chairman)
Hon CHAN Kin-por, JP (Deputy Chairman)
Hon Albert HO Chun-yan
Ir Dr Hon Raymond HO Chung-tai, SBS, S.B.St.J., JP
Hon James TO Kun-sun
Dr Hon Philip WONG Yu-hong, GBS
Hon Emily LAU Wai-hing, JP
Hon Abraham SHEK Lai-him, SBS, JP
Hon Vincent FANG kang, SBS, JP
Hon LEE Wing-tat
Hon Jeffrey LAM Kin-fung, SBS, JP
Hon Andrew LEUNG Kwan-yuen, GBS, JP
Hon WONG Ting-kwong, BBS, JP
Hon Ronny TONG Ka-wah, SC
Hon CHIM Pui-chung
Hon KAM Nai-wai, MH
Hon Starry LEE Wai-king, JP
Dr Hon LAM Tai-fai, BBS, JP
Hon Mrs Regina IP LAU Suk-ye, GBS, JP

Member attending : Hon WONG Kwok-hing, MH

Members absent : Dr Hon David LI Kwok-po, GBM, GBS, JP
Hon Paul CHAN Mo-po, MH, JP

Public officers attending : Agenda Item IV

Mr John TSANG, GBM, JP
Financial Secretary

Mrs Helen CHAN, JP
Government Economist

Mr Arthur AU
Administrative Assistant to Financial Secretary

Agenda item V

Miss Natalie LI
Principal Assistant Secretary for Financial Services
and the Treasury (Financial Services)⁵

Ms Karen KEMP
Executive Director (Banking Policy)
Hong Kong Monetary Authority

Ms Rita YEUNG
Head (Banking Policy) A
Hong Kong Monetary Authority

Ms Rose LUK
Head (Banking Policy) C
Hong Kong Monetary Authority

Clerk in attendance : Ms Anita SIT
Chief Council Secretary (1)⁵

Staff in attendance : Mr Noel SUNG
Senior Council Secretary (1)⁵

Ms Haley CHEUNG
Legislative Assistant (1)⁵

I Confirmation of minutes of meetings and matters arising

(LC Paper No. CB(1)2319/10-11 — Minutes of special meeting on 1 March 2011

LC Paper No. CB(1)2346/10-11 — Verbatim record of special meeting on 21 April 2011)

The minutes of the special meeting held on 1 March 2011 and the verbatim record of the special meeting held on 21 April 2011 were confirmed.

Motion regarding regulation of derivative warrants market

2. Mr James TO opined that the motion on regulation of the derivative warrants market he had proposed at the special meeting on 23 May 2011 should be discussed under this agenda item as a matter arising from the previous meeting, instead of being discussed under the last agenda item of "Any other business".

3. Mr Andrew LEUNG remarked that as the motion was not voted on at the last meeting because of the absence of a quorum, the present arrangement of dealing with the motion under the agenda item of "Any other business" of this meeting was appropriate.

4. The Chairman put the matter to vote. Five members supported that the motion should be dealt with under the agenda item "Any other business", whereas three members supported dealing with the motion under the present agenda item as a matter arising from a previous meeting. Given the voting result, the Chairman remarked that Mr James TO's motion regarding regulation of derivative warrants market would be dealt with under the agenda item "Any other business".

II Information papers issued since the last meeting

(LC Paper No. CB(1)2323/10-11(01) — Submission dated 24 May 2011 from the Association for the Advancement of Feminism on regulation of listing of overseas corporations in Hong Kong (Chinese version only))

5. Members noted the information papers issued since the last regular meeting on 9 May 2011.

III Date of next meeting and items for discussion

(LC Paper No. CB(1)2040/10-11(01) — List of outstanding items for discussion

LC Paper No. CB(1)2040/10-11(02) — List of follow-up actions

LC Paper No. CB(1)2104/10-11(01) — Letter dated 5 May 2011 from Hon James TO Kun-sun (Chinese version only)

Meeting in July 2011

6. Members agreed to discuss the following items at the next regular meeting scheduled for 4 July 2011:-

- (a) Detailed proposals for the establishment of an independent Insurance Authority;
- (b) Proposal of the Securities and Futures Commission for a short position reporting regime; and
- (c) Professional Accountants (Amendment) Bill 2011.

Members noted that items (a) and (b) were proposed by the Administration whereas item (c) was proposed by Mr Paul CHAN.

IV Briefing by the Financial Secretary on Hong Kong's latest overall economic situation

(LC Paper No. CB(1)2181/10-11(01) — First Quarter Economic Report 2011 and the press release

LC Paper No. CB(1)2361/10-11(03) — Administration's paper on Hong Kong's recent economic situation and near-term outlook)

Briefing by the Administration

7. At the invitation of the Chairman, the Financial Secretary (FS) briefed members on the latest economic situation by highlighting the following -

- (a) The International Monetary Fund had maintained in April 2011 its projected global economic growth for 2011 at 4.4%. The global economy was experiencing a two-speed recovery. The emerging markets, especially the Asian economies, were the major driving force for the global economy. The fundamentals in the developed economies such as the US and European countries remained relatively weak.
- (b) Hong Kong's economy sustained strong momentum in the first quarter of 2011, with real GDP leaping by 7.2% over a year earlier. Growth in the first quarter was slightly higher than the already appreciable 7.0% growth for 2010 as a whole, marking the fifth consecutive quarter that growth was distinctly above the average annual growth over the past 10 years. On a seasonally adjusted quarter-to-quarter comparison, GDP grew by 2.8% in real terms in the first quarter, the eighth consecutive quarter of expansion.
- (c) Total exports of goods resumed the strong uptrend in the first quarter, surging by 16.8% in real terms over a year earlier. Yet total exports of goods slowed considerably in April 2011, due partly to the incidents in Japan. This highlighted the need of staying vigilant of external uncertainties. Exports of services likewise stayed buoyant in the first quarter. Exports of financial and other business services surged on the back of strong growth in cross-border financing and sustained external demand for Hong Kong's commercial and professional services. Exports of trade-related services grew notably further in tandem with vibrant regional trade flows. Exports of travel services likewise grew apace, thanks to strong tourist arrivals from Asia as a whole and further increase in arrivals from the long-haul markets. The incidents in Japan had to a certain extent affected the offshore trading and exports of transportation services.
- (d) Domestically, consumer sentiment was well supported by the improving job and income situations and to some extent by the further increases in asset prices. The volume of total retail sales leaped by 21.9% in April over a year earlier, reflecting the still-buoyant consumption market. The implementation of a number of major infrastructure projects also rendered additional support to domestic demand, yet due to the fall-back in the volatile private machinery and equipment investment, overall investment spending relapsed to a year-to-year decline in the first quarter. Business sentiment however stayed sanguine.

- (e) The labour market saw further broad-based improvement in early 2011 amid the robust economic conditions. The current unemployment rate of 3.5% was two percentage points lower than the peak seen during the global financial crisis, and was only slightly above the post-1977 low of 3.3%. However, as a new batch of graduates and school leavers would enter the labour market in the coming months, and the implementation of the statutory minimum wage might also encourage more people to seek jobs, these would augment the labour force, thus posing some pressure on the unemployment rate. Labour earnings in the first quarter of 2011 showed notable improvement. Average employment earnings for the lowest decile of full-time employees rose by 6.2% in nominal terms or by 2.0% in real terms.
- (f) In the light of the better than expected economic performance in the first quarter, even allowing for some possible moderation in the rest of the year, GDP growth for 2011 as a whole should exceed the forecast of 4-5% made in February 2011, and was revised upwards to 5-6% in May 2011.
- (g) In spite of the strong growth momentum thus far this year, there were external uncertainties which might pose risks to the local economy. These included the unsteady economic recovery in the US, the deterioration of the sovereign debts problem in Europe, the more stringent macro economic policies imposed by Asian economies, heightened geopolitical risks in the Middle East and North Africa, and the repercussions of the natural disasters and nuclear incidents in Japan. While the US Federal Reserve had indicated that the second round of quantitative easing (QE2) would be completed as scheduled by end of June this year, the actual exit time might vary as the pace of the US economic recovery remained unsteady. In the period ahead, market expectations on the US interest rates might shift and global fund flows might also reverse, thereby heightening financial market volatilities and risks. From Hong Kong's perspective, one of the key concerns was that interest rates would eventually revert to increase after staying at low levels for an extended period. This would exert pressure on the local asset markets, and in turn undermine consumption and investment sentiment and even the performance of the real economy. The Government would closely monitor all these relevant developments and remain vigilant.

- (h) Rising inflation was a major challenge that Hong Kong had to face in the foreseeable future. The underlying inflation rate was 4.4% in April 2011, higher than the 3.7% recorded in the first quarter of 2011. Indeed, inflation had become a common challenge faced by Asian economies with vibrant growth. Both domestic and external factors adding to local inflation would not subside in the near term. On the external front, global commodity and food prices continued to soar. Domestically, upward pressures on local costs had increased after five quarters of very rapid economic growth, and with the one-off effect arising from the implementation of the statutory minimum wage, inflation was likely to go up further in the coming months. The forecast rates of headline and underlying consumer price inflation for 2011 as a whole were revised upwards to 5.4% and 5.5% respectively, from 4.5% as announced earlier. The Government was concerned about the local inflation situation, particularly its impact on low-income households.
- (i) The Government paid close attention to the property market situation and the related asset bubble risk. After the introduction of the Special Stamp Duty in November 2010, speculation activities had subsided. The number of property transactions had dropped from 13 200 transactions in November 2010, to the average of 9 200 transactions per month in the first five months of 2011, i.e. a drop of about 30%. The extremely low interest rate and abundant liquidity, coupled with robust economic growth, had continued to push property prices upward to surpass the peak in 1997. As flat prices continued to rise at a faster pace than income, the home purchase affordability ratio soared to around 49% in the first quarter of 2011, which was only slightly lower than the long-term average of 51% over 1990-2009. The Government had recently bolstered its effort in increasing land supply. In addition to the Application List system, the Government had put up additional sites for auction and tender. In the first two months of this financial year, six residential sites had already been sold, with the tenders for two sites providing flats of specified sizes being processed. The nine residential sites put up for sale in the first quarter of the financial year would provide nearly 3 000 residential flats. The Government would continue to announce our land sale programme in advance on a quarterly basis, including both residential and non-residential sites. The Development Bureau had already drawn up the list of sites to be sold in the second quarter of 2011-12 financial year, and would announce the details shortly. The site on top of the West Rail Nam

Cheong Station would also be put up for tender in the next quarter. The total number of flats which would be developed on the sites sold in the next quarter would exceed that of the current quarter. The Government would study ways to provide usable land to meet Hong Kong's housing and economic development needs in the medium to long term. The Development Bureau had initiated public discussion on the possibility of reclamation outside Victoria Harbour, and rock cavern development.

- (j) The Hong Kong Monetary Authority (HKMA) had stepped up examination of banks' mortgage businesses. In order to ensure that the banks would manage the risks of mortgage loans properly, HKMA had introduced measures in October 2009, August 2010 and November 2011, to tighten the loan-to-value ratios for mortgage loans and require banks to conduct stress tests of interest rate hike on applicants for mortgage loans. HKMA was considering measures to further tighten up mortgage loan requirements in order to enhance risk management among local banks. The Government would closely monitor the development of the property market, including transaction figures in both the primary and secondary markets for residential flats, the mortgage loan statistics, and the transaction prices of land auctions and tenders. Where the situation warranted, the Government would not hesitate to introduce further measures to ensure the stable and healthy development of the property market. Members of the public should take into consideration the external economic environment and the trend of interest rates, and assess their own affordability when making decisions on purchase of properties.

(Post-meeting note: The Government's press release (in Chinese only) on FS's above opening remarks (LC Paper No. CB(1)2435/10-11(01)) was issued to Members on 10 June 2011.)

8. The Government Economist (GE) gave a Powerpoint presentation on the latest developments in the Hong Kong economy, the updated economic forecasts for 2011, and the latest situation of low-income households.

(Post-meeting note: The presentation notes (LC Paper No. CB(1)2452/10-11(01)) were issued to Members by a Lotus Notes e-mail on 13 June 2011.)

Discussion

Property market

9. Noting that the average property price had exceeded the 1997 price level, Mr WONG Kwok-hing enquired whether the Government would impose additional land sale conditions restricting the unit sizes of the residential flats to be developed on the sites concerned, and requiring the developers to accord priority to first time buyers who purchased the flats for self-use.

10. FS pointed out that the Government had not ever imposed such restrictions on the buyers of private residential properties, as such restrictions might adversely affect Hong Kong's status as an international financial centre and the long term development of Hong Kong's economy. Given that Hong Kong had an open and free economy, the Government had to be very cautious in considering proposals of imposing restrictions on the buyers of residential properties, as it would involve a major change in policy.

11. Mr Jeffrey LAM was concerned that the property market might have a "hard landing" when the interest rates resumed the upward trend, possibly in early or mid-2012. In view that property prices remained high despite the anti-speculation measures introduced by the Government, Mr LAM enquired whether the Government had conducted any assessment of the effectiveness of the Special Stamp Duty as a measure to curb speculation and prevent the formation and burst of a property market bubble.

12. FS responded that the US interest rates were expected to rise eventually once the US economic recovery gathered pace, and the interest rates in Hong Kong would follow the trend in the US. Based on the Government's analysis, an increase of the existing interest rate by 3 percentage points would lead to a lift of the affordability ratio to 63%, exceeding the long term average of 51% for the past 20 years. Given that home purchase was a major investment decision for many people, prospective home buyers should be very careful in making their investment decisions. They should be aware of the impact on their repayment abilities when interest rates eventually rose back. The Government would continue to identify sites from the Application List for government-initiated sale to increase the supply of housing land.

13. Mr LEE Wing-tat remarked that it was alarming that property prices had already passed the 1997 level, and the affordability ratio had reached nearly 50%. Mr LEE opined that if the Government could ensure that about 20 000 to 30 000 residential units would be available in the market in the coming year as promised in the 2011-2012 Budget, through measures such as increased supply of land, it would help stabilise property prices. Mr LEE was of the view that if a condition could be included in the land leases that the residential units developed on the sites might only be sold to first time residential property buyers, with additional restrictions such as a means test on the prospective buyers, it would help the first time home buyers like the young people, and such

an arrangement would not violate the free market principle. Mr LEE remarked that when time and again the FS said that measures would be introduced to curb speculation in the property market as and when necessary, and yet property prices continued to rise, the public would take the statements lightly until and unless the measures took effect.

14. FS responded that while he had repeatedly warned investors about the volatile economic situation and the risks involved, the Government had introduced successive packages of measures to curb speculation in the property market. The measures implemented, including those introduced in November 2010, had proved to be effective in curbing speculation in the property market. In addition to the Application List system, the Government had put up additional sites for auction with a view to increasing the supply of land and stabilising the property market. The number of sites to be identified for sale in the next quarter would exceed that in the current quarter, and the Government would continue to announce the land sale programme in advance on a quarterly basis. He would discuss with the Secretary for Transport and Housing on Mr LEE's suggestion of giving first time local buyers priority in the sale of residential units.

15. The Deputy Chairman pointed out that the affordability ratio had been maintained at above 60% for a long time from 1989 to 1998, and there did not seem to be an automatic and direct correlation between a high affordability ratio and a property market bubble.

16. FS explained that the macro environment in the 1990s was drastically different in the sense that interest rates were much higher in the 1990s, whereas interest rates would only go up in the current episode given the extraordinarily low interest rates at the moment. As such, the impact of an increase in interest rates on the affordability ratio could be larger.

17. While expressing concern about the rising property prices, Ms Starry LEE enquired whether the Government had maintained any statistics regarding the purchase of local residential units by Mainland buyers and the types of residential units involved. Ms LEE opined that the Government should consider setting up a database on the purchase of local residential units by non-Hong Kong residents, as there was a general view that the upsurge in property prices was very much attributable to the investment from overseas and Mainland buyers.

18. FS explained that it was difficult to maintain statistics on the number of local residential units purchased by Mainland buyers, because their investments could be made through different channels. According to the information from the trade, buyers from the Mainland usually purchased first-hand and high-end residential units.

19. Dr LAM Tai-fai expressed grave concern that the affordability ratio of mortgage loan borrowers had reached 49%, and with the anticipated increase in interest rates, the ratio would further go up, leading to the burst of the property market bubble and widespread negative equity. Dr LAM pointed out that prospective property buyers were in a dilemma in considering whether they should acquire a property, given that property prices might continue to soar or the property market bubble might burst. Dr LAM enquired whether the Government considered that the current affordability ratio of 49% was healthy, and if not, what measures would be taken to forestall the escalation of the ratio, and what advice FS would give to the public to face the situation.

20. FS pointed out that the existing affordability ratio of 49% could go up to 63% should the existing interest rate rise by 3 percentage points. FS further added that local banks had increased mortgage interest rates several times recently, and with the end of QE2 in the US by end of June 2011 as well as increasing external uncertainties including the slower pace of economic recovery in the US and the deepening crisis from the euro zone sovereign debt problem, members of the public should be cautious in assessing their affordability when purchasing properties.

21. Mr James TO remarked that despite the anti-speculation measures so far introduced by the Government, property prices had continued to soar. Members of the public who had a reasonable expectation of owning their own homes felt disappointed. Since the Government had rejected the proposal to impose restriction on non-Hong Kong residents in purchasing local properties, and the increase in land supply did not seem to have material effect on the soaring property prices, the only alternative available to counteract the heated property market seemed to be the resumption of the Home Ownership Scheme (HOS). Mr TO was of the view that it was unlikely that the provision of a few thousand HOS units each year would lead to the collapse of the property market. In the worst scenario, only a small number of property owners might face the problem of negative equity. Mr TO enquired whether the Government would re-consider resuming the construction of HOS flats. Mr TO opined that applicants who had been on the public housing waiting list for seven years should be given priority to buy the Home Ownership Scheme flats.

22. FS stressed that the Government had considered all factors involved and consulted parties concerned before formulating its present policy on the HOS. In his Policy Address made in October 2010, the Chief Executive had announced the introduction of an enhanced scheme of subsidised housing known as the "My Home Purchase Plan" to cater for the need of specific groups. The Chief Executive noted the demands regarding the resumption of

the HOS and he would follow up this issue in his Policy Address in October 2011.

Rental control and public housing

23. Mr Albert HO expressed concern that despite the anti-speculation measures introduced by the Government, property prices continued to soar and many people, including the newly wedded couples, were forced to rent their homes. These people still had to face the problem of increasing rentals, and might never be able to save sufficient money to purchase their own homes. Mr HO enquired whether the Government would consider re-introducing rental control which had been cancelled since 2002/2003. Mr HO pointed out that the amount of rental subsidies granted under the various social security schemes also lagged behind the rise in rentals.

24. FS responded that the Government had reviewed the need for introducing rental control measures, and given that such measures would distort the operation of the free market, the Government had no plan to reintroduce them. FS pointed out that the introduction of the Special Stamp Duty had the effect of stabilizing the rentals of private residential flats.

25. Mr Albert HO enquired, in view of the long time required for allocation of public housing and the rising rentals, whether the Government would consider designating more sites for development of public housing units to meet the demand.

26. FS responded that the Government would endeavour to ensure an adequate supply of land to produce about 15 000 public housing flats each year, thus maintaining an average waiting time of three years.

27. Mr LEE Wing-tat pointed out that the rentals for shops and commercial premises had surged considerably recently, by a margin of 40% to 50%, which might impede the development of new and small businesses, and result in large enterprises dominating all business sectors.

28. FS responded that it could be an unhealthy state of affairs if the business sectors were dominated by large enterprises and the Government would closely monitor the situation. He pointed out that the significant increases in rentals and transactions for shops and commercial premises were mainly a result of the improved economic situation. GE supplemented that compared with last year, the rentals for shops and offices in March 2011 had increased by 8.6% and 12.4% respectively. When compared with the pre-crisis peak in 2008, the latest rentals for shops had increased cumulatively by only 11% whereas the rentals for offices had just returned to the 2008 peak. The upsurge in rentals for

commercial premises was mainly supported by the strong demand in tandem with the vibrant economy, considering that the value of total retail sales had leaped by 28% in April over a year earlier. In response to the rising demand for commercial premises, the Government had also increased the number of sites for commercial/hotel development in the Application List. The Government would continue to monitor the situation closely.

Employment

29. Noting that more than 200 000 persons still had to rely on the support of the Comprehensive Social Security Assistance scheme, Mr WONG Kwok-hing enquired whether the Government would consider providing sites in some districts of Hong Kong for use by street traders, in order to improve the livelihood of the poor.

30. FS responded that the unemployment rate had dropped to a relatively low level of 3.5% and job seekers should not have much difficulty in finding a job. It was doubtful whether it was the appropriate time to introduce the measure proposed by Mr WONG.

31. Noting that the overall employment between February to April 2011 increased by 102 300 compared with 2010 trough, and of which, 24 300 were lower-skilled workers, the Deputy Chairman enquired about the factors contributing to the increase in job openings, and the relevant fields where jobs had been created for lower-skilled workers.

32. GE responded that with the continued improvement of the overall economic situation and with real GDP leaping by 7.2% in the first quarter over a year earlier, more jobs had been created. Employment situation improved across nearly all sectors, in particular the import and export, food and retail businesses, and the tourism and hotel industry which engaged a large number of lower-skilled workers.

33. The Chairman expressed concern that while the implementation of the statutory minimum wage had improved the employment conditions of many lower-skilled workers, there were claims that many lower-skilled workers had lost their jobs with the implementation of the statutory minimum wage. Mr Jeffrey LAM shared the Chairman's concern and enquired whether the Government had undertaken an assessment of the impact of the statutory minimum wage on the unemployment rate.

34. GE responded that as the statutory minimum wage was just implemented as from 1 May 2011, its impact on the employment situation had yet to be ascertained. GE said that she would include in the next briefing an analysis of

the employment situation in different sectors, with particular focus on those sectors which employed a large number of lower-skilled workers, such as the retail and food business, security and cleansing service sectors and hence which were more affected by the implementation of the statutory minimum wage.

Inflation

35. Mr Ronny TONG expressed grave concern about rising inflation, which would reach 5% in the year, and the impact of the soaring prices in transport, food and accommodation on the livelihood of the general public, especially the low income groups. Given that Hong Kong was constrained in adjusting its exchange and interest rates to counteract rising inflation, Mr TONG enquired what measures the Government would take to help the public to meet the challenges of inflation. Mr TONG opined that instead of giving a sum of \$6,000 to Hong Kong Permanent Identity Card holders aged 18 or above, the Government should consider providing subsidies to the public on transport, food and accommodation expenses, in order to relieve the inflationary pressure on the public.

36. FS reiterated that inflation was a major concern of the Government, and in the 2011-2012 Budget, he had introduced a series of measures to relieve the pressure of inflation on the public, including the provision of an electricity charge subsidy, paying two months' rent for public housing tenants and waiving rates. With the increase in their actual income, members of the public would be in a better position to meet the challenges of inflation. FS added that similar to the situation of Hong Kong, many economies in the Asian region were facing the common challenge of rising inflation.

37. Ms Starry LEE remarked that despite the improvement of the economic situation, the public was still subject to economic pressure arising from the rapid upsurge of property prices and the inflation rate, including the increases in food and fuel prices. Ms LEE enquired whether the Linked Exchange Rate system was one of the main factors contributing to rising inflation in Hong Kong.

38. FS explained that the rising inflation did not stem from the Linked Exchange Rate system. Many economies in the Asian region which did not have a linked exchange rate system also faced rising inflation. The rising inflation was mainly a result of the global commodity price upsurge, food prices in particular, caused by global liquidity glut and strong demands from the emerging economies. The experience of some economies revealed that the appreciation of currencies and interest rate hikes could not help much in offsetting the pressure of inflation.

V Briefing on progress of implementation of Basel II enhancements and plan to implement Basel III

(LC Paper No. CB(1)2361/10-11(04) — Administration's paper on "Progress in Implementation of Basel II Enhancements and Plan to Implement Basel III"

LC Paper No. CB(1)2360/10-11 — Background Brief on the implementation of Basel II and Basel III in Hong Kong prepared by the Legislative Council Secretariat)

Briefing by the Administration

39. The Executive Director (Banking Policy), Hong Kong Monetary Authority (ED(BP)/HKMA) briefed members, through a Powerpoint presentation, on the progress of implementation of the enhancements to the Basel II regulatory capital framework issued by the Basel Committee on Banking Supervision (BCBS) in July 2009, the new regulatory capital and liquidity standards issued by BCBS in December 2010 (known as Basel III) and the plan to implement Basel III in Hong Kong starting from 1 January 2013.

(Post-meeting note: The presentation notes (LC Paper No. CB(1)2459/10-11(01)) were issued to Members by a Lotus Notes e-mail on 13 June 2011.)

Discussion

40. Mr Abraham SHEK enquired how the Basel II enhancements and Basel III measures would help to uphold the stability of Hong Kong's financial market in face of a major financial crisis, given that the Basel II regime had been found to be inadequate to meet the challenges of a global financial crisis.

Mr SHEK expressed concern about the financial implications of implementing the Basel II enhancements and Basel III, and the impact on the business development and competitiveness of Hong Kong, and the impact on authorized institutions (AIs), customers of AIs and small and medium sized enterprises (SMEs). Mr SHEK further enquired about the consequence of not implementing the Basel II enhancements and Basel III requirements in Hong Kong.

41. ED(BP)/HKMA pointed out that the global financial crisis broke out in 2008 before the Basel II measures had been fully rolled out. The global financial crisis, nevertheless, had revealed certain deficiencies within the Basel II framework and the need to regularly review banking supervision requirements in the light of changing business models in the banking sector. ED(BP)/HKMA remarked that while the more stringent capital and liquidity requirements would inevitably increase the operating costs of AIs, the new measures should make AIs more resilient in the face of any future financial crisis. ED(BP)/HKMA pointed out that AIs took into account not only the Basel requirements but a host of other factors, including market competition, in setting the price levels for loans and financial products. Hong Kong was a member of the BCBS, and, as such, should implement the Basel II enhancements and Basel III requirements. After the outbreak of the global financial crisis, international bodies such as the Financial Stability Board had put strong emphasis on regulatory reforms, and had been closely monitoring the implementation of the reforms in different jurisdictions. If Hong Kong, as an international financial centre, failed to implement the Basel II enhancements and Basel III requirements, Hong Kong might face the risk of being listed as a non-compliant jurisdiction and its future participation in international bodies might be jeopardized.

42. The Deputy Chairman expressed concern that the implementation of the Basel II enhancements and the Basel III requirements might adversely affect the profitability of AIs, in particular the small and medium sized AIs.

43. ED(BP)/HKMA reiterated that the objective of the Basel II enhancements and Basel III requirements was to enhance the resilience and risk management capability of AIs, which might potentially help reduce the AIs' funding costs and hence lending costs. The capital requirements and the profitability of AIs might not always be directly correlated as the profitability of AIs could be affected by various factors. AIs might be put in a disadvantageous position vis-à-vis their peers overseas if they did not follow international practices and comply with the latest supervisory requirements for the banking sector.

44. In view that the international credit rating agencies had acted slowly in adjusting the crediting ratings of financial institutions during the recent global financial crisis, the Deputy Chairman enquired how the implementation of the Basel II enhancements and Basel III would help improve recognition of counterparty credit risk.

45. ED(BP)/HKMA responded that part of the Basel III arrangements were designed to reduce the reliance of financial institutions on credit ratings, and encourage the banks to conduct their own independent assessments on the credit worthiness of their counterparties based on a variety of factors, rather than relying solely on the ratings assigned by credit rating agencies.

VI Any other business

Motion on regulation of derivative warrants market

(LC Paper No. CB(1)2361/10-11(05) — Wording of motion proposed to be moved by Hon James TO but not dealt with at the meeting on 23 May 2011

LC Paper No. CB(1)2421/10-11(01) — Paper provided by the Hong Kong Exchanges and Clearing Limited on the results of the buyback offer made by Goldman Sachs Structured Products (Asia) Limited in respect of the four derivative warrants linked to the Nikkei 225 Index)

46. The Chairman drew members' attention to the following motion moved by Mr James TO at the special meeting held on 23 May 2011, which was not voted on owing to the absence of a quorum at the material time of the meeting.

"本事務委員會不滿政府、證監會和港交所到現時為止的處理方法。本事務委員會要求上述機構與相關發行人繼續商討合理與公平的解決方案。"

(Translation)

"That this Panel is not satisfied with the way in which the Government, SFC and HKEx have handled the matter so far, and requests the above authorities to continue the discussion with the relevant issuer for a reasonable and fair resolution."

47. The Deputy Chairman remarked that he did not consider that the Panel was not satisfied with the way in which the Government, Securities and Futures Commission (SFC) and Hong Kong Exchanges and Clearing Company (HKEx) Limited had handled the matter so far. He said that he only supported that the Government, SFC and HKEx should be requested to continue the discussion with the relevant issuer for a reasonable and fair resolution of the matter. The Deputy Chairman said that he would abstain from voting on the motion.

48. Mr Abraham SHEK said that as he did not have knowledge of all the details of the incident, he would not support or object to the motion.

49. The Chairman put Mr James TO's motion to vote. Four members voted for the motion. The Deputy Chairman and Mr Abraham SHEK abstained from voting. The Chairman declared that the motion moved by Mr James TO was passed.

(Post-meeting note: The Administration's response to the motion was issued to members vide LC Paper No. CB(1)2775/10-11 on 19 July 2011.)

50. There being no other business, the meeting ended at 4:50 pm.

Council Business Division 1
Legislative Council Secretariat
25 August 2011