



HONG KONG MONETARY AUTHORITY

**Briefing to the Legislative Council  
Panel on Financial Affairs**

**5 May 2014  
[Translation]**



- 1. Assessment of Risk to Hong Kong's Financial Stability**
2. Development of Financial Market
3. Banking Supervision
4. Investment Performance of the Exchange Fund



## **ASSESSMENT OF THE US ECONOMY**

- The US economy and labour market continue to improve
- The Fed may end its asset purchase programme this autumn
- A great majority of Fed officials expect interest rates to rise in mid-2015
- Whether labour market faces cyclical or structural problems remains to be seen
- Both the extent and pace of rate rises are highly uncertain

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## **ASSESSMENT OF THE EURO AREA ECONOMY**

- Economic contraction ceases, with slow recovery and persistently low inflation
- Public, private and banking sectors all saddled with high debts
- Yet market sentiment remains sanguine, with decent performance in the equity and bond markets
- European Central Bank is willing to adopt more aggressive measures to tackle low inflation

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## ASSESSMENT OF JAPAN'S ECONOMY

- Economic recovery continues but wage growth remains weak and current account continues to worsen
- Bank of Japan may introduce a second round of quantitative and qualitative easing (QQE) if the consumption tax hike poses a greater-than-expected drag on the economy
- Some progress with Abe's "third arrow" on structural reforms but the most important part is yet to be agreed on
- Massive public debt still a major risk to Japan's economy

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## ASSESSMENT OF MAINLAND CHINA'S ECONOMY

- Growth momentum softened, while the Government's economic growth target for 2014 was set at around 7.5%
- Daily trading band of the RMB/USD exchange rate was widened from 1% to 2% in mid-March
- The Government pledged to continue to contain financial risks as well as to strengthen the monitoring of default risks in local government financing platforms, industries with overcapacity and the real estate sector
- Foreign institutions have two different views on Mainland's economic outlook:
  - Many analysts at financial institutions are relatively pessimistic, with greater focus on financial risks associated with local government financing platforms and "shadow banking"
  - Multinational firms with operations in the Mainland are generally more optimistic, and believe that there is still enormous potential in the Mainland market

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## ASSESSMENT OF GLOBAL ECONOMIC AND FINANCIAL STABILITY RISKS

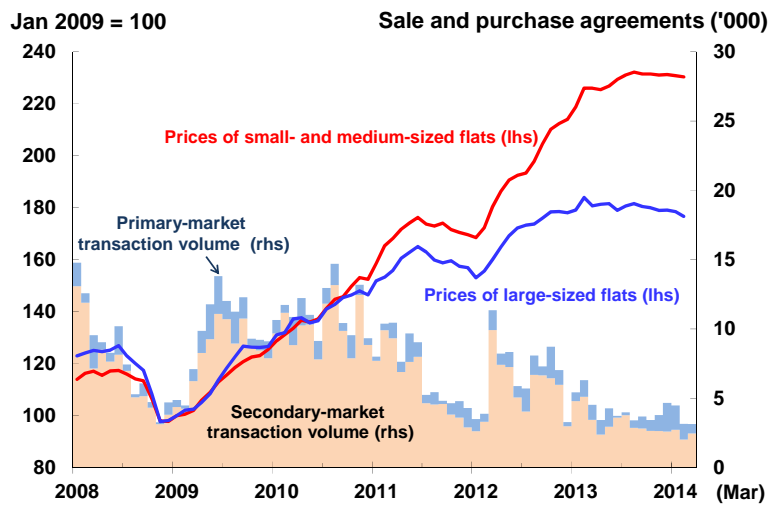
- Market sentiment turning more positive, which may have underestimated potential risks
- The Fed will continue to reduce asset purchases but the timing, extent and pace of rate rises remain uncertain
- The US monetary normalisation process would put pressure on capital flows in emerging markets
- As the rate-hike cycle draws near, risk to interest rates and asset price movements in emerging markets increases

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## ASSESSMENT OF RISK ON HONG KONG'S FINANCIAL STABILITY: PROPERTY MARKET

### Property market under consolidation, but outlook still uncertain

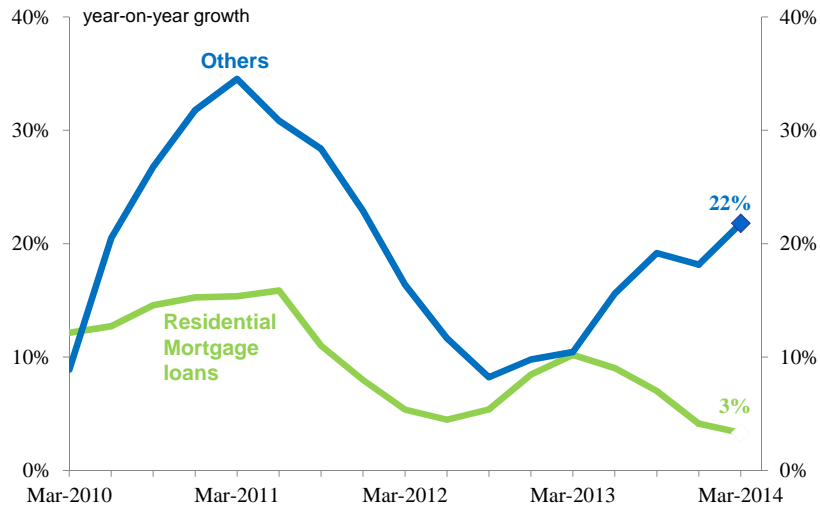


Sources: R&VD and Land Registry

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## HONG KONG FINANCIAL STABILITY RISK ASSESSMENT: CREDIT EXPANSION



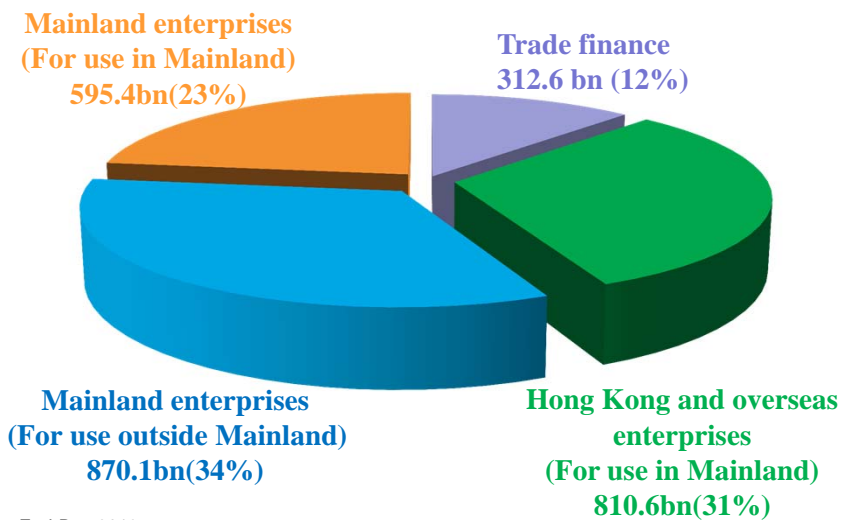
Note : Other loans do not include residential mortgage loans and IPO financing

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## HONG KONG FINANCIAL STABILITY RISK ASSESSMENT: MAINLAND-RELATED LENDING

Total : 2,588.7bn



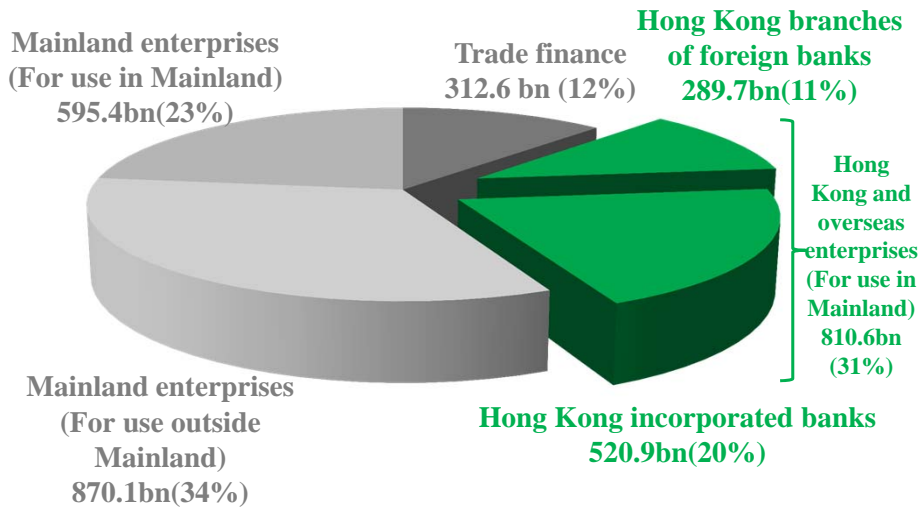
Position : End-Dec 2013

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## MAINLAND-RELATED LENDING

Total : 2,588.7bn



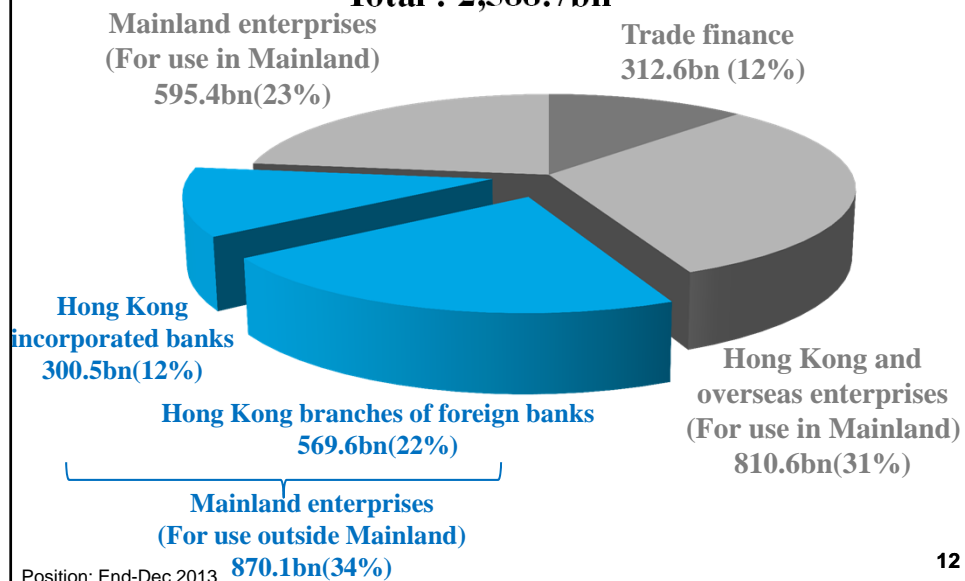
Position : End-Dec 2013

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## MAINLAND-RELATED LENDING

Total : 2,588.7bn



Position: End-Dec 2013

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## MAINLAND-RELATED LENDING

Total : 2,588.7bn

Mainland enterprises (For use in Mainland)

595.4bn (23%)

Hong Kong incorporated banks

484.1bn (19%)

Hong Kong branches  
of foreign banks

111.3bn (4%)

Trade finance

312.6bn (12%)

Mainland enterprises  
(For use outside Mainland)  
870.1bn (34%)

Hong Kong and overseas  
enterprises  
(For use in Mainland)  
810.6bn (31%)

Position : End-Dec 2013

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## RISK MANAGEMENT

- **Areas for attention**
  - Accelerating pace of loan growth since 2010
  - Mainly driven by Mainland-related lending
- **Supervisory principle**
  - Focus on banks' risk management systems
  - ✓ Credit risk management : Ensure prudent credit underwriting standards
  - ✓ Liquidity risk management : Stable Funding Requirement
- **Loan quality remains good: Overall risks manageable**

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## **DEVELOP HONG KONG AS A CORPORATE TREASURY CENTRE (CTC)**

- Financial Secretary has set up a task force to review the taxation of corporate treasury activities under the Inland Revenue Ordinance in order to attract multinational corporations to set up their CTCs in Hong Kong. The task force will come up with concrete proposals in 12 months
- HKMA will liaise with the industry stakeholders and proactively participate in the work of the task force. We will also continue to promote Hong Kong as a destination for CTCs

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## DEVELOPMENT OF ISLAMIC FINANCE

- The Loans Ordinance has been amended to provide a legal basis for issuance of Islamic bonds (sukuk) under the Government Bond Programme
- Likely to be the world's first Islamic bond issued by an AAA rated Government
- Working closely with the Government in formulating a detailed plan for the inaugural Government sukuk. The preliminary plan is as follows:
  - Issuance size : US\$500 million – US\$1 billion
  - Tenor : 5 years or below
  - Target investors : International institutional investors
  - Sukuk structure : Lease (underlying assets : Government-owned properties in commercial premises)
  - Listing : Seek listing status in Hong Kong and major Islamic financial centres

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## **INTERNATIONAL STANDARDS TO DEAL WITH “TOO-BIG-TO-FAIL” FINANCIAL INSTITUTIONS**

- Legislative reform to meet international standards: Financial Stability Board (FSB)’s “Key Attributes of Effective Resolution Regimes”
- Fill gaps in HK regulators’ existing toolkits to support resolution of failing financial institutions
- Three-month public consultation closed on 6 April 2014; 33 submissions received
- Proactive stakeholder engagement during consultation period
- Second consultation exercise later in 2014, with a view to implementation by FSB’s end-2015 deadline

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## **BASEL III IMPLEMENTATION PROGRESS**

### **Legislative changes in Q4 2014**

- Banking (Capital) (Amendment) Rules 2014
- Banking (Disclosure) (Amendment) Rules 2014
- Banking (Liquidity) Rules

### **Consultations**

- Countercyclical capital buffer
- Higher loss absorbency for systemically important banks

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## INVESTMENT INCOME

	2014	2013	2012	2011
(HK\$ billion)	Q1*	Full Year	Full Year	Full Year
<b>Hong Kong equities<sup>@</sup></b>	<b>(6.8)</b>	<b>10.1</b>	<b>30.7</b>	<b>(24.2)</b>
<b>Other equities</b>	<b>3.6</b>	<b>71.8</b>	<b>42.8</b>	<b>(12.2)</b>
<b>Bonds</b>	<b>13.2</b>	<b>(19.1)</b>	<b>33.1</b>	<b>71.9</b>
<b>Other investments<sup>&amp;</sup></b>	<b>-</b>	<b>16.8</b>	<b>6.4</b>	<b>0.7</b>
<b>Foreign exchange</b>	<b><u>1.1</u></b>	<b><u>1.6</u></b>	<b><u>(1.4)</u></b>	<b><u>(9.1)</u></b>
<b>Investment income<sup>@&amp;</sup></b>	<b>11.1</b>	<b>81.2</b>	<b>111.6</b>	<b>27.1</b>

\* Unaudited figures

<sup>@</sup> Excluding valuation changes in Strategic Portfolio

<sup>&</sup> Including valuation changes of private equity and real estate investments held by Exchange Fund's investment holding subsidiaries

(The first quarter valuation change is not available pending the receipt of valuation reports of some investments)

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## INCOME AND EXPENDITURE

(HK\$ billion)	2014	2013				
	Q1*	Full year	Q4	Q3	Q2	Q1
<b>Investment income/(loss)</b>	<b>11.1</b>	<b>81.2</b>	<b>30.7</b>	<b>54.7</b>	<b>(23.3)</b>	<b>19.1</b>
Other income	-	0.2	-	0.1	0.1	-
Interest and other expenses	<u>(1.1)</u>	<u>(4.9)</u>	<u>(1.2)</u>	<u>(1.3)</u>	<u>(1.5)</u>	<u>(0.9)</u>
Net income/(loss)	10.0	76.5	29.5	53.5	(24.7)	18.2
<b>Payment to Fiscal Reserves#</b>	<b>(7.1)</b>	<b>(36.8)</b>	<b>(9.0)</b>	<b>(9.0)</b>	<b>(9.5)</b>	<b>(9.3)</b>
Payment to HKSAR government funds and statutory bodies#	(1.9)	(9.3)	(2.6)	(2.5)	(2.1)	(2.1)

\* Unaudited figures

# The fixed rate of fee payment is 3.6% for 2014 and 5.0% for 2013

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