立法會
Legislative Council

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Panel on Financial Affairs

Minutes of special meeting
held on Monday, 11 May 2009 at 11:30 am
in the Chamber of the Legislative Council Building

Members present :
Hon CHAN Kam-lam, SBS, JP (Chairman)
Hon Ronny TONG Ka-wah, SC (Deputy Chairman)
Hon James TO Kun-sun
Dr Hon Philip WONG Yu-hong, GBS
Hon Abraham SHEK Lai-him, SBS, JP
Hon Vincent FANG kang, SBS, JP
Hon Jeffrey LAM Kin-fung, SBS, JP
Hon Andrew LEUNG Kwan-yuen, SBS, JP
Hon WONG Ting-kwong, BBS
Hon CHIM Pui-chung
Hon KAM Nai-wai, MH
Hon Starry LEE Wai-king
Hon Paul CHAN Mo-po, MH, JP
Hon CHAN Kin-por, JP
Hon Mrs Regina IP LAU Suk-yee, GBS, JP

Members absent :
Hon Albert HO Chun-yan
Dr Hon David LI Kwok-po, GBM, GBS, JP
Hon Emily LAU Wai-hing, JP
Hon Tanya CHAN

Public officers attending :
Agenda item I

Prof K C CHAN, SBS, JP
Secretary for Financial Services and the Treasury

Miss AU King-chi, JP
Permanent Secretary for
Financial Services and the Treasury
(Financial Services)

Mr Clement LEUNG, JP
Deputy Secretary for
Financial Services and the Treasury (Treasury) 2

Mr Edmond LAU, JP
Executive Director (Monetary Management)
Hong Kong Monetary Authority

Mr Daryl HO
Head (Market Development) (Acting)
Hong Kong Monetary Authority

Clerk in attendance: Ms Rosalind MA
Chief Council Secretary (1)5

Staff in attendance : Mr Noel SUNG
Senior Council Secretary (1)4

Ms Haley CHEUNG
Legislative Assistant (1)8

Action

I Government Bond Programme

(LC Paper No. CB(1)1507/08-09(01) — Letter dated 5 May 2009 to the Administration

LC Paper No. CB(1)1507/08-09(02) — The Administration's supplementary information on Government Bond Programme

G6/123/5C — The Legislative Council Brief issued by the Financial Services and the Treasury Bureau

LC Paper No. CB(1)1469/08-09(01) — The Administration's paper on Government Bond Programme

LC Paper No. CB(1)1559/08-09(01) — The Administration's presentation material on Government Bond Programme (tabled at the meeting and soft copy issued on 11 May 2009) (Chinese version only)

LC Paper No. CB(1)1558/08-09(01) — Dr Hon David LI's letter dated 8 May 2009 (tabled at the meeting and issued to members on 12 May 2009) (Chinese version only))

Briefing by the Administration

At the invitation of the Chairman, Secretary for Financial Services and the Treasury (SFST) advised that the Government aimed to promote the further and sustainable development of the local bond market and enhance the breadth, depth and liquidity of the market through launching a regular and systematic government bond programme (GBP). In response to the Panel's request at the meeting held on 4 May 2009, the Government had provided supplementary information on the considerations for launching and details of implementing GBP (LC Paper No. CB(1)1507/08-09(01)). SFST pointed out that the proposed framework of GBP had been drawn up having regard to government bond programmes of overseas economies and views of market participants. In view of Members' comments on the details of GBP and the setting up of a subcommittee to study the two proposed resolutions for the implementation of GBP (the Subcommittee), SFST advised that the Financial Secretary (FS) had withdrawn the notices given for moving the motions regarding the proposed resolutions at the Council meeting on 20 May 2009. SFST further said that the Government would work closely with the Subcommittee to facilitate the latter’s scrutiny of the proposed resolution.

2. Head (Market Development) (Acting) Hong Kong Monetary Authority (H(MD)/HKMA) gave a powerpoint presentation on the proposed framework of GBP, including mechanism for executing GBP, determination of yields for government bonds, and the possible benefits to investors.

Discussion

3. The Chairman drew members' attention to the letter of Dr David LI tabled at the meeting (LC Paper No. CB(1)1558/08-09(01)), expressing support to the implementation of GBP for the development of the local bond market.

Considerations for the launch of GBP

4. Mr CHIM Pui-chung expressed support for GBP in principle but doubted whether investors' confidence and interest in government bonds would be adversely affected by the Lehman Brothers-related Minibonds fiasco. He questioned whether the Government had a comprehensive plan for implementing GBP taking into account the impact of bond issuance on the securities market. Mr CHIM also expressed reservation on possible investors' response to the government bonds given the expected unattractive yield amid the prevailing low interest rate environment.

5. Mr James TO opined that the Government should also take into account the total quantity of bonds to be issued by other public organizations and the impact of GBP on other issuers in the market when designing the parameters of GBP.

6. SFST responded that the government bonds to be issued under GBP were different in nature from the Lehman Brothers-related Minibonds, the latter being complicated structured financial products comprising underlying collaterals subject to an array of default risks. Bonds to be issued under GBP were high quality investment instruments with stable return. SFST advised that in the implementation of GBP, the Government would give careful consideration to the timing and size of issuance, taking into account factors including the prevailing market conditions, investor demand and pricing of the bonds. SFST further pointed out that issuance of government bonds under GBP was not expected to have any abrupt impact on the bond market given the modest size of each bond issuance.

7. While expressing support in principle to GBP, Mrs Regina IP was concerned about the considerations for the timing of launching GBP. She queried the reasons for the Government to seek implementation of GBP in such a hasty manner, and doubted whether the Government had proposed the issuance of government bonds as an attempt to restore investors' confidence in the investment in bonds in the aftermath of the Lehman Brothers-related Minibond fiasco. She asked whether the current low interest rate environment was conducive to the Government's decision for early implementation of GBP. Mrs IP opined that Members of the Legislative Council (LegCo) should be given adequate time to examine details of the implementation framework before passing the relevant resolutions for the implementation of GBP.

8. SFST stressed that government bonds would be issued on an on-going and long-term basis under GBP to promote the further and sustainable

development of the local bond market. The interest rate environment was only one of the considerations in determination of the timing for launching GBP. He advised that as the Government had been studying and considering measures to promote the development of local bond market having regard to overseas practices and experience of past bond issuance exercises, it had been able to work out the proposed framework for implementation of GBP shortly after the relevant announcement by FS in his 2009-2010 Budget Speech. Nevertheless, the Government had not set any rigid schedule for moving the motions regarding the relevant resolutions. There would be sufficient time for LegCo to consider the proposed framework of GBP.

9. Referring to the considerations for the launch of GBP in the supplementary information provided by the Government, Mr KAM Nai-wai sought elaboration on whether it was the right time for launching GBP.

10. SFST said that given the current investment environment in which investors were looking for high quality products with stable return, bonds issued under GBP were expected to be well-received by the market, in particular the institutional investors. As such, the Government considered it an opportune time to launch GBP. Permanent Secretary for Financial Services and the Treasury (Financial Services) (PS(FS)) supplemented that a well-developed government bond market was often seen as a necessary pre-condition for the development of the corporate bond market. The growth of the Hong Kong dollar bond market driven by the on-going and systematic issuance of government bonds could also help meet the demand of institutional investors such as pension funds and insurance companies for Hong Kong dollar assets to match with their long-term Hong Kong dollar liabilities. In the light of, inter alia, investors' interest in government bonds amid the volatile market, the Government considered it an opportune time to launch GBP.

11. Mr CHAN Kin-por expressed support for GBP to promote the development of the bond market. He said that the insurance industry welcomed the issuance of government bonds to provide Hong Kong dollar assets to match with their long-term Hong Kong dollar liabilities. He called on the Government to expedite implementation of GBP to make good use of the current low interest rate environment and to meet the demand of investors. On the issuance size, Mr CHAN opined that the proposed borrowing ceiling of HK$100 billion should be increased if there was favourable market response to GBP.

12. SFST said that in drawing up the proposed overall issuance size of GBP, a prudent approach was adopted. The borrowing ceiling of HK$100 billion represented a long-term target to be achieved in five to ten years. He reiterated that the objective of GBP was to promote the further and sustainable development of the local bond market, attracting more investors to the local

bond market to provide the necessary conditions for the development of, for instance, the corporate bond market.

Types of bonds to be issued

13. Mr Jeffrey LAM expressed support for GBP to develop the bond market which would be key to reinforcing Hong Kong's status as an international financial centre. Noting that the Government would not rule out the possibility of adding more variety to the types of bonds to be issued under GBP, Mr LAM asked whether bonds for financing infrastructural projects and Renminbi (RMB)-denominated bonds would be issued. Mr CHAN Kin-por opined that consideration should be given to issuing RMB-denominated bonds under GBP to meet the demand of the insurance industry for RMB assets.

14. SFST responded that the Government intended to issue only fixed rate bonds with a simple structure and denominated in Hong Kong dollar at the initial implementation stage of GBP. Other types of bonds might be issued at a later stage of implementation if the issuance was considered beneficial to promoting the development of the local bond market. Given the policy objective of GBP to develop the Hong Kong dollar debt market, SFST advised that the Government had no plan to issue RMB-denominated bonds at this stage. SFST also said that sums raised under GBP would not be used for financing infrastructural projects as sufficient public resources would be provided for these projects. Responding to Mr Jeffrey LAM's further enquiry on the tenor of the bonds to be issued under GBP, SFST advised that bonds of tenors within a range of two to ten years would likely be issued at the initial stage of GBP, with a view to providing a diversified tenor mix to meet market demand. In the long run, consideration would be given to issuing bonds with a longer tenor, The Government would continue to tap market views when drawing up the details for individual issuances under GBP.

Investment of the Bond Fund

15. The Deputy Chairman was of the view that as there was no need for the Government to raise funds to finance public expenses, there was no urgency for it to issue government bonds through GBP. Noting that the proceeds raised under GBP would be credited to the Bond Fund, to which the investment strategies of the Exchange Fund (EF) and the "fixed rate" sharing arrangement would apply, the Deputy Chairman expressed concern about the investment risks involved. In this connection, he noted that while the compound annual investment return of EF in the years 1994 to 2008 was 6.1%, there had been great fluctuations in the rates of return during the period. He therefore sought further information on the expected investment risks of the moneys in the Bond Fund.

16. Mr James TO was concerned whether investment gain could be guaranteed if the Bond Fund adopted the investment strategies of EF, and whether the investment returns would be sufficient to meet the financial obligations and liabilities associated with GBP.

17. SFST said that placing the Bond Fund with EF for investment would be appropriate as the two funds shared similar investment objectives, i.e. to preserve capital and generate reasonable investment returns. The long-term and conservative investment strategies of EF could serve the need of the Bond Fund as the investment risk would be averaged out over a longer term. The "fixed rate" sharing arrangement applicable to the Bond Fund was expected to provide a stable investment return for the Bond Fund. Executive Director (Monetary Management)/Hong Kong Monetary Authority (ED(MM)/HKMA) supplemented that the "fixed rate" sharing arrangement meant that investment return for the Bond Fund in any one year would be determined in accordance with the average rate of return of EF's investment portfolio over the past six years or the average annual yield of three-year Exchange Fund Notes for the previous year, whichever was the higher. Deputy Secretary for Financial Services and the Treasury (Treasury) 2 added that given the "fixed rate" sharing arrangement, the Government expected that moneys in the Bond Fund should be adequate to meet the financial obligations and liabilities associated with GBP. In the very unlikely event of any shortfall in the Bond Fund, the Government would seek LegCo's approval for transfer of funds from the general revenue to the Bond Fund in accordance with paragraph (c) (iii) of the proposed resolution under section 29 of the Public Finance Ordinance (Cap.2).

18. Mr James TO queried whether the government bonds to be issued under GBP would be principal-guaranteed, as there might be shortfall in the Bond Fund to meet the financial obligations and liabilities associated with GBP should the investment of the Bond Fund suffered great losses and the Government could not obtain the approval of LegCo for appropriation from the general revenue to meet the shortfall.

19. The Deputy Chairman and Mr KAM Nai-wai expressed concern about the administrative and fund management costs incurred for placing the Bond Fund with EF for investment. In reply, ED(MM)/HKMA advised that HKMA would not charge to the Bond Fund administrative or staff costs incurred for implementation of GBP and investment of the sums raised under GBP, except for expenses arising from the necessary procurement of services from financial institutions or other third party by HKMA for the offering of bonds.

20. Mr WONG Ting-kwong supported the implementation of GBP to meet the demand for government debt securities in the market. Noting that the sums raised under GBP would be invested by HKMA in accordance with the investment strategies of EF, Mr WONG was concerned about the oversight mechanism to ensure proper management and investment of the Bond Fund.

Mrs Regina IP expressed a similar view. Mrs IP was also concerned about the administrative costs incurred for the offering of bonds under GBP.

21. SFST responded that under the proposed framework of GBP, FS would direct HKMA to assist the Government in coordinating the offering of bonds, and to invest moneys in the Bond Fund in accordance with the investment strategies of EF. HKMA would make use of the existing market infrastructure and experience for issuance of Exchange Fund Bills and Notes (EFBN) for GBP. Such an arrangement could minimize the administrative costs incurred for implementation of GBP. The proposed "fixed rate" sharing arrangement would also provide the Bond Fund with a stable investment return for meeting the financial obligations and liabilities associated with GBP. Responding to Mr Abraham SHEK's concern about who would be accountable for the implementation of GBP, SFST said that the Government as a whole was responsible.

Yields for the government bonds

22. The Deputy Chairman enquired about the determination of yields for the bonds to be issued under GBP. Mr KAM Nai-wai and Mr Abraham SHEK raised similar enquiry, in particular for retail tranches. In reply, SFST advised that the yields of the bonds would be determined by prevailing market conditions such as the interest rate environment at the time of issuance. The pricing mechanism of retail bonds to be issued under GBP would follow the market convention but the exact interest rate benchmark to be used had yet to be determined. Responding to Mr KAM's further enquiry, ED(MM)/HKMA provided for Members' reference the yields of two-year US Treasury (0.94% to 0.95%) and two-year EFBN (0.56% to 0.57%). ED(MM)/HKMA nevertheless stressed that the yields of government bonds would have to be determined in accordance with the prevailing market conditions at the time of issuance.

23. Responding to the Deputy Chariman's enquiry about bond prices in the secondary market, SFST advised that bond price in the secondary market might fluctuate according to changes in interest rates in the market. In general, if interest rates rose, bond prices would fall and vice versa. Individual investors could mitigate the risk of incurring trading loss due to fluctuations in interest rates by holding the bond until maturity when they could collect the full sum of the principal, and would have earned the interests paid according to the coupon rate of the bond.

24. Mr James TO was concerned about the mechanism to safeguard the reasonable price fixing of the bonds to be issued under GBP. In this connection, Mr TO asked the Government to consider measures such as prescribing the maximum yield for the government bonds in the legislation. In reply, SFST pointed out that the price of the government bonds would be

determined by the market. Market forces would make the price of the government bonds close to the market interest rates even if legislative or administrative measures were put in place to fix the price of the bonds at issuance. SFST further advised that similar to previous bond issuance exercises, issuance of bonds under GBP should follow market convention in order to promote the development of the local bond market.

25. Mr Vincent FANG expressed support for GBP to strengthen Hong Kong's position as an international financial centre. Mr FANG asked the Government to consider issuing a larger proportion of bonds for the retail tranche to meet the demand of retail investors for products of lower risk and more stable return. While appreciating that the yields for the government bonds would be determined by the market, Mr FANG sought information on the range of possible yields for reference.

26. SFST responded that the Government had not set any fixed proportion of bonds intended for institutional and retail tranches respectively. The exact size of individual bond issues and the proportion for each tranche would be determined having regard to relevant factors including the prevailing market conditions, market demands, and impact on other issuers in the market. ED(MM)/HKMA supplemented that if there was strong demand for a retail issue, consideration could be given to increasing the size of that particular issue or offering an additional issue shortly, according to common market practices. As for the yields of government bonds, SFST reiterated that these would be determined by the market. He could not forecast the market interest rates at the time of bond issuance and therefore was unable to provide such information at the present stage. ED(MM)/HKMA supplemented that market conditions would vary over time and it would be difficult to provide a reasonable projection at this stage.

Mechanism for offering government bonds

27. Mr Abraham SHEK expressed support for GBP in principle but requested the Government to allow sufficient time to respond to Members' concerns before implementation. Pointing out that some $20 billion worth of government bonds had been issued in previous securitization exercises, Mr SHEK queried whether the borrowing ceiling of $100 billion proposed for GBP would be sufficient to promote the development of the local bond market.

28. SFST responded that GBP was an on-going programme aimed at increasing the size of the local debt market, which was different from previous one-off issuances on ad hoc basis. The regular and systematic issuance of bonds under GBP would attract more investors and thus enhancing liquidity of the bond market, allowing the market to grow into a critical mass. In response to Mr Abraham SHEK's view that the Government should make reference to the mechanism for offering bonds in the securitization exercise in 2004,

H(MD)/HKMA advised that as far as he understood, the offering mechanism used in the 2004 exercise mainly followed the commercial operation of appointing bank syndicate and distributing banks for the global sale of bonds, which was appropriate for a one-off issuance exercise. For the on-going issuance of bonds under GBP, the proposed offering mechanism had been drawn up with reference to those of government bond programmes in other economies. Instead of appointing bank syndicate for the offering of government bonds, the Government had proposed to offer the institutional tranche of government bonds by way of competitive tender opened to Primary Dealers to be appointed by HKMA.

29. Mr Abraham SHEK expressed views from the investor protection angle on bonds to be issued under GBP. Mrs Regina IP also expressed views on issues relating to investor protection, such as risk disclosure to investors, investor education and training of frontline staff in the sale of bonds to retail investors. In response, SFST advised that the Government was committed to adhering to a high level of transparency and information disclosure for the bonds to be issued under GBP. The Government would make reference to common industry standards when preparing the offering documents to facilitate investors in making informed investment decisions. PS(FS) supplemented that in coordinating the offering of bonds under GBP, HKMA would follow the established tendering procedures and be subject to the relevant regulatory requirements enforced by the Securities and Futures Commission on the offering and sale of bonds, such as disclosure requirements.

30. To ensure fair arrangements in the offering of government bonds, Mr TO suggested that the Government set out in the proposed resolution under section 3 of the Loan Ordinance (Cap.61) that the government bonds would be distributed in a "fair and reasonable" manner.

Use of moneys in the Bond Fund

31. On the use of sums raised under GBP, Mr Vincent FANG and Mr WONG Ting-kwong shared the view that the sums should be used for investing in public works projects to revive the economy of Hong Kong. This was similar to the arrangement in the securitization exercise of "five tunnels and one bridge" in 2004. In reply, SFST pointed out that the Government had made clear its financial commitment for implementation of public infrastructure projects in the next five to ten years. The sums raised under GBP would not be required for funding such projects. He further advised that the securitization exercise of "five tunnels and one bridge" was a one-off exercise, which was different from the long-term, on-going and systematic nature of GBP. The setting up of the Bond Fund was thus considered appropriate for managing sums raised under GBP. The Bond Fund would be managed separately from the fiscal reserves and other government accounts, enabling clear presentation and ready assessment of the financial performance

of GBP. This could also provide clear information to investors on the Bond Fund's ability to meet the financial obligations and liabilities associated with GBP.

Way forward

32. Pointing out that the investing public was unfamiliar with the local bond market, the Chairman asked the Government to provide more information on the operation of the local bond market to facilitate Members' consideration of the proposed resolutions for the implementation of GBP. He also opined that, in addition to the conventional fixed rate bonds, the Government should consider issuing other types of bonds under GBP to promote market development and liquidity in the secondary bond market.

33. SFST took note of Members' views. He assured Members that the Government would work closely with the Subcommittee and provide necessary information to facilitate the latter's scrutiny of the proposed resolutions for the implementation of GBP.

II Any other business

34. There being no other business, the meeting ended at 1:22 pm.

Council Business Division 1
Legislative Council Secretariat
28 August 2009