

**Economic Summit on
“China’s 11th Five-Year Plan and the Development of Hong Kong”
(11 September 2006)**

**Summary of Views Expressed at Focus Group Discussion on
Financial Services**

Overview

Panelists discussed the suitable financial development strategy for Hong Kong in response to the 11th Five-Year Plan and associated challenges and opportunities, with the aim of enhancing the status of Hong Kong as an international financial centre.

2. Panelists considered the relationship between the two financial systems of Hong Kong and the Mainland should be cooperative, complementary and interactive. While there are challenges brought about by the reforms of Mainland financial system under the 11th Five-Year Plan, Hong Kong’s strong financial platform still has much to offer to the Mainland, in terms of helping to improve the efficiency of the financial intermediation and support sustainable economic growth on the Mainland. On the other hand, increased use of Hong Kong for Mainland international financial activities would help enhance Hong Kong as an international financial centre (paragraphs 5-6).

3. Panelists also discussed a five-pronged financial development strategy (paragraphs 7-15). They agreed that Hong Kong could help improve the efficiency of Mainland financial intermediation by strengthening Hong Kong services to both the international and domestic financial intermediation on the Mainland. Further, Hong Kong could provide a testing ground for renminbi to become convertible.

4. Panelists proposed that apart from the Mainland market, Hong Kong should proactively explore business opportunities on financial services in other economies of the Asia-Pacific region (paragraphs 16-20). In response to the discussions, panelists agreed to set up three working groups to study specific strategies to be put forward in the action agenda (paragraph 21).

Challenges and Opportunities Presented by the 11th Five-Year Plan

5. Panelists agreed that as reforms of Mainland financial system under the 11th Five-Year Plan were implemented, Hong Kong's status as an international financial centre could face the following challenges –

- (a) with the improvement of equity and bond markets on the Mainland, companies could make use of such markets to raise funds, reducing the use of Hong Kong's markets;
- (b) when renminbi was fully convertible, offshore investors could invest in the Mainland financial markets directly, reducing the need to do so through Hong Kong;
- (c) when financial markets on the Mainland were fully liberalised, financial activities might migrate to the then larger and more liquid Mainland markets; and
- (d) when renminbi became an international currency, there would be competition from other financial centres in the region on providing renminbi-denominated financial services.

6. However, if Hong Kong could move with the times, the implementation of the 11th Five Year Plan might also present opportunities for Hong Kong –

- (a) Hong Kong could strengthen its role in financial intermediation between the Mainland and the rest of the world. Located within the Asia time zone, Hong Kong had a comparative advantage in serving as the platform for channelling foreign capital into the Mainland. Hong Kong could also provide services for offshore investments by Mainland institutions and individuals;
- (b) Hong Kong could participate in domestic financial intermediation activities on the Mainland. First, for financial services to be provided on location, the vast market on the Mainland offered a great deal of development potential for Hong Kong's financial institutions. Second, as Mainland's capital account was liberalised, Hong Kong could provide a convenient, reliable and efficient platform for Mainland investors and

fund-raisers to meet, thereby channelling Mainland savings to the hands of Mainland fund-raisers; and

- (c) Hong Kong could provide a testing ground for renminbi internationalisation, which was only a matter of time. Hong Kong should strive to be the first mover and develop into a commercial and financial centre for trade and financial transactions settled in renminbi outside the Mainland.

A Five-Pronged Financial Development Strategy

7. In response to the above challenges and opportunities, Panelists agreed that Hong Kong, while continuing to preserve its sound financial system, and further increase the depth and breath of our financial markets, should adopt the following five-pronged strategy.

Further increasing the presence of Hong Kong financial institutions in the Mainland market

8. Through CEPA and other channels, Hong Kong's financial institutions should expand their range of services and actively develop their business on the Mainland. In particular, Hong Kong's financial institutions could contribute by providing transfer of technical know-how and a greater variety of financial instruments and services on the Mainland.

Further facilitating funds, investors, fund-raisers and financial institutions on the Mainland to come out and link up with the global market

9. This would strengthen Hong Kong's role in financial intermediation between the Mainland and the rest of the world, by serving not just inflows to but also outflows from the Mainland. Particularly, given that Mainland investors were more familiar with the efficient financial markets in Hong Kong, Hong Kong could provide an effective channel for orderly outflows of funds from the Mainland. Moreover, Hong Kong could serve as a springboard for Mainland financial institutions to develop their international business.

Bringing financial instruments issued in Hong Kong to the Mainland

10. To make financial instruments issued in Hong Kong available in the Mainland would not only provide Mainland investors with more

investment tools but also allow Mainland enterprises, particularly those from the Pearl River Delta area, to improve their corporate governance through listing in Hong Kong, while at the same time helping the development of Hong Kong's financial markets.

11. Allowing financial instruments between two markets to be fungible in a gradual manner could also reduce the price differential of same shares and promote harmonisation of regulatory standard across the border.

Further expansion of renminbi business in Hong Kong, particularly in respect of trade settlement in renminbi and the issuance of renminbi bonds

12. As financial activities conducted by Mainland investors and fund-raisers were denominated in renminbi, Hong Kong needed to enhance the capability of its financial system to handle renminbi-denominated transactions. As a first step, the Government should continue pushing ahead for the expansion of renminbi business in Hong Kong, which could proceed in tandem with the process of moving towards renminbi convertibility for capital account items on the Mainland.

Strengthening cross-border linkage of payment systems and settlement and clearing systems for equity and bonds

13. To facilitate cross-border fund flows, monitor the associated risks and enhance the efficiency of financial intermediation and supervision, there was a need to strengthen financial infrastructural linkages between Hong Kong and the Mainland. At present, the financial infrastructural linkages between Hong Kong and the Mainland were first forged through Guangdong and Shenzhen. This underscored the strategic importance of Guangdong in financial cooperation between the Mainland and Hong Kong. Further studies on regional linkages in support of Guangdong's planning should be conducted.

14. Panelists agreed that strengthening the cooperation between the regulatory bodies in Hong Kong and the Mainland was a prerequisite for the implementation of the above five-pronged strategy. In this context, the Government should seek to work closely with the Mainland authorities regarding the country's financial reform and reflect views on how Hong Kong can contribute to the country's financial reform and development as appropriate.

15. The Hong Kong Monetary Authority would prepare a detailed proposal on how each of the above five strategies should be best pursued.

Other Suggestions

16. Panelists proposed that apart from the Mainland market, Hong Kong should explore the business opportunities in other economies in the region. Hong Kong could be more out-reaching in promoting our financial services to the rest of the world. In particular, panelists pointed out Taiwan and other Southeast Asian economies as the main targets that our financial institutions should focus on. Hong Kong has been faring well in attracting other companies in such economies to list in Hong Kong, and given the improving economic outlook, more quality companies in the region will seek listings in well-recognized stock exchanges. Panelists agreed that efforts should be devoted in facilitating these companies to list in Hong Kong.

17. In addition to our dedication to the equity market, panelists also mentioned the importance of developing full-fledged financial markets in Hong Kong. The 11th Five-Year Plan mentioned the gradual development of a commodities futures market. In this connection, panelists recommended the Government to examine whether and how the commodities futures market should be developed in Hong Kong. Since China had already become one of the largest consumers in commodities and raw materials in the world, it was in the interest of our country to have Hong Kong becoming an international commodities futures market as soon as possible. A panelist suggested Hong Kong to set up an oil exchange market to facilitate Mainland's energy companies to trade in Hong Kong.

18. Panelists also emphasised that the Government's policy must retain a strong pool of talents, both groomed locally or recruited globally to maintain Hong Kong's high standard of financial and related services. Panelists recommended the Government to further relax its immigration policies to facilitate more Mainland talents to pursue a career in Hong Kong, and maintain its comparative advantages over other regional competitors, in particular its low tax regime and higher living standard.

19. As to the further development of the insurance industry in Hong Kong, the rapid development of the Mainland had generated much demand for insurance and re-insurance. Since Hong Kong was one of the most

open insurance and re-insurance markets in the world, panelists recommended that Hong Kong's insurance practitioners should explore the business opportunities therein, and continue to foster mutual exchanges with its Mainland counterparts.

20. Panelists also discussed the benefits of further expanding the presence of asset management industry in Hong Kong. The high saving rates as well as the huge amount of money in the Asia-Pacific region provide tremendous potential for Hong Kong's asset management industry. Also, it is generally agreed that Hong Kong has the fundamentals to develop as an international hedge funds centre. Hong Kong should consider facilitating the setting-up of international hedge funds through, on an ongoing basis, refining its licensing and regulatory requirements. But we should also be careful about the potential risks that such funds might bring to the stability of our financial system.

Way Forward

21. Panelists agreed that, in addition to the specific proposals to be worked on by the Hong Kong Monetary Authority for the five-pronged strategy, three working groups would be set up, each headed by one of the Focus Group members to study specific strategies to be put forward in the Action Agenda –

- (a) the working group headed by the Honourable Ronald Arculli would study the listing rules and regulations in order to facilitate further development of our local equity market;
- (b) the working group headed by Mr He Guangbei would study further development of Hong Kong's foreign exchange, futures and commodities trading; and
- (c) the working group headed by Mr Tse Sze-wing, Edmund would study further development of the insurance and reinsurance industries in Hong Kong and the Mainland. The working group would also study ways to attract more pension funds, university endowment and private foundation funds to be set up and invest locally with a view to further strengthening and developing Hong Kong as an international asset management centre.

22. The Focus Group would work out in the next few months specific recommendations along this specific direction and submit an action plan to the Chief Executive for consideration.
23. The attendance list is attached.

Central Policy Unit
October 2006

金融服務專題小組
2006年9月11日

Focus Group on Financial Services
11 September 2006

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Apologies

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