Chapter 4

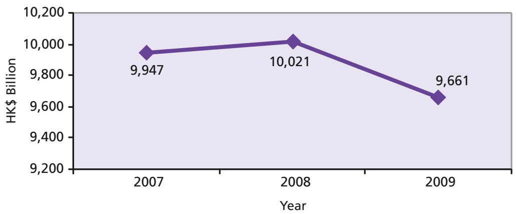
Financial and Monetary Affairs

Hong Kong ranks among the world's top financial centres, thanks to its well established and regulated banking, securities and insurance industries. Its stock exchange ranked seventh globally and third in Asia in terms of market capitalisation. Hong Kong also led the world in raising funds through initial public offerings (IPOs) in 2009. The financial sector has a 213 400-strong workforce, or 5.8 per cent of the city's total workforce, and contributes 16.1 per cent of the city's GDP.

Hong Kong is a vibrant international financial centre invigorated by a sophisticated financial infrastructure, world-class financial professionals, a regulatory regime as good as any in the world, high liquidity and efficiency. The Government's aim is to reinforce further Hong Kong's position as an international financial centre in general and as a capital formation centre, an offshore Renminbi (RMB) centre and an asset management centre particularly by making continuous improvements to the regulatory system, promoting corporate governance, strengthening investor protection, fostering market development and enhancing links and co-operation with the Mainland.

Hong Kong made a number of major achievements in 2009. These included:

Chart 1 External Positions of Authorised Institutions (AIs)



Being the world's 15th and Asia's 3rd largest banking centre in terms of external positions[1]. and the world's 6th largest centre for foreign exchange trading.

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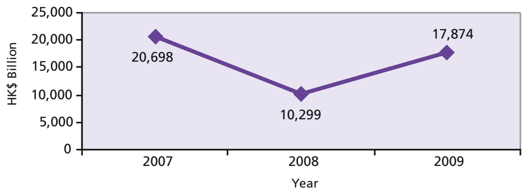
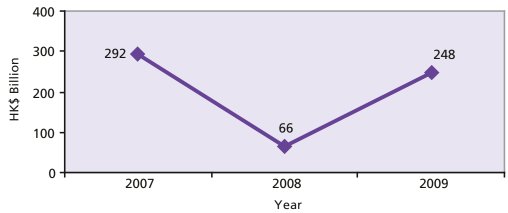
1 Sum of liabilities to banks and non-bank customers outside Hong Kong and claims on banks and non-bank customers outside Hong Kong (such as equities, securities and capital instruments).

Chart 2 Market Capitalisation of Stock Market



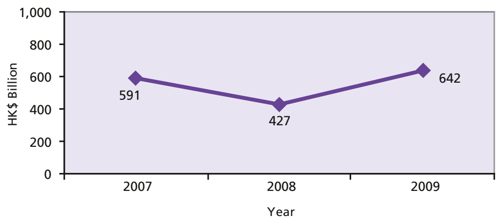
Hong Kong's stock exchange being ranked 7th in the world and 3rd in Asia in terms of market capitalisation which rose by 74 per cent to $17,874 billion in 2009.

Chart 3 Equity Funds Raised Through IPOs



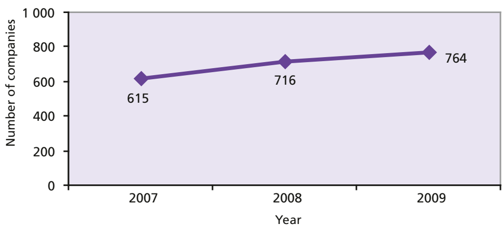
Being the stock market that raised $248 billion through IPOs in 2009, more than any bourse in the world.

Chart 4 Total Equity Funds Raised in HK



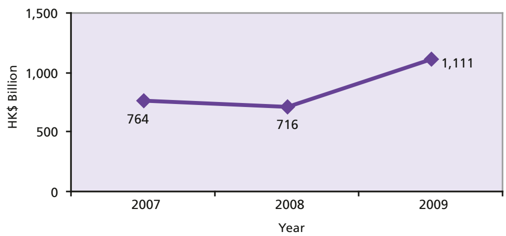
Ranking 4th in the world and 2nd in Asia as a stock exchange in terms of total equity funds raised which amounted to $642 billion in 2009.

Chart 5 Number of Asset Management Companies in HK



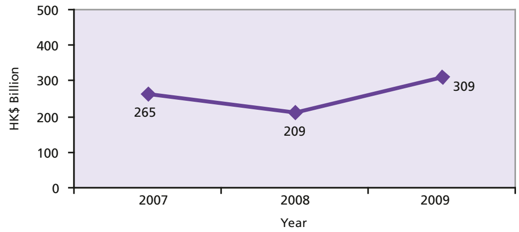
764 companies are licensed or registered to conduct asset management business in Hong Kong in 2009, an increase of 48 companies, or 7 per cent over 2008.

Chart 6 Total Outstanding HKD Debt Securities



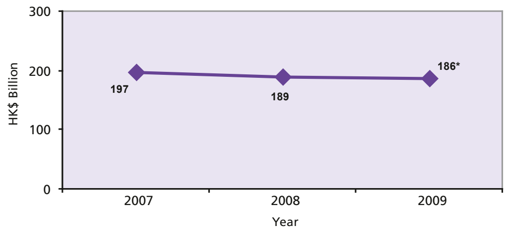
Having outstanding Hong Kong dollar debt securities, including exchange fund bills and notes, totalling $1,111 billion at year end, or 55 per cent up on the previous year's $716 billion.

Chart 7 Total NAV of MPF Assets



Net asset values (NAV) of Mandatory Provident Fund (MPFs) schemes topped $309 billion at the end of 2009 with an annualised internal rate of return of 5 per cent since its inception in 2000.

Chart 8 Annual Gross Premiums of Insurance Market



Staying the course as one of the most open insurance markets in the world, achieving an annual premium growth of 6 per cent during the past three years. The total gross premiums of Hong Kong's insurance market remained steady at $185.7* billion in 2009.

Hong Kong as an International Financial Centre

Overview

Hong Kong as a leading international financial centre in the region is helped by a favourable geographical location, bridging the time gap between New York and London; strong links with the Mainland and economies in Southeast Asia and excellent communication with the rest of the world; the rule of law; a level playing field for conducting business and a sound regulatory regime. The absence of restrictions on capital flows into and out of Hong Kong is another advantage.

Hong Kong's financial markets are highly liquid. They operate under effective and transparent regulations, which are in line with international standards. A highly educated workforce and ease of entry for professionals from outside Hong Kong also contribute to the development of its financial markets.

International financial institutions maintain a strong presence in the city. Of the world's top 100 banks, 69 have operations in Hong Kong. At the end of the year, 135 of the 145 licensed banks in Hong Kong were foreign-owned.

The interbank money market is well established. Wholesale deposits are traded actively among local Authorised Institutions (AIs), and between local and overseas institutions, with an average daily turnover of $226.7 billion in 2009.

The last triennial survey co-ordinated by the Bank for International Settlements in 2007 shows the daily average foreign exchange turnover in Hong Kong at US$174.6 billion, making Hong Kong the world's sixth largest foreign exchange market.

* Provisional statistics

With a total market capitalisation of about $17,874 billion at year's end, the Hong Kong stock market ranked seventh in the world and third in Asia. The daily turnover averaged $62.3 billion in 2009. At year's end, 1 319 public companies were listed on the Stock Exchange of Hong Kong (SEHK). The 68 newly listed companies on the Main Board raised $247.9 billion from IPOs.

In 2009, Hong Kong ranked first worldwide in terms of IPO funds raised. Besides new share issues, $393.9 billion were raised on the secondary market.

The Hong Kong stock market is an important fund-raising platform for Mainland enterprises. At year's end, there were 524 Mainland enterprises listed on the SEHK. In 2009, equity funds raised by Mainland enterprises[2] amounted to $346 billion, which was 55 per cent of the total equity funds raised through the SEHK during the year. About $201 billion was raised in new listings of Mainland enterprises in Hong Kong, accounting for 83 per cent of the total equity funds raised in IPOs on the SEHK.

Overseas intermediaries were increasingly interested in setting up business operations in Hong Kong. The number of Stock Exchange Participants[3] (SEPs) increased from 449 at the end of 2008 to 463 at the end of 2009. The futures market also saw an increase in the number of Futures Exchange Participants (FEPs), from 148 at the end of 2008 to 167 at the end of 2009. Among the SEPs and FEPs, 156 and 74 respectively were owned by non-Hong Kong interests. In 2009, 19 SEPs and 22 FEPs were newly admitted, including those from France, India, Korea, Switzerland, the Mainland, the Netherlands, the United Kingdom and the United States, and Taiwan.

The asset management industry is characterised by its strong international flavour, in terms of the presence of both global fund managers and the different domiciles of authorised funds. At year's end, 764 companies were licensed or registered to carry out asset management business, representing an increase of 7 per cent from a year earlier. In addition to the Securities and Futures Commission (SFC) licensed corporations, banks and insurance companies also participate in asset management business.

Hong Kong operates one of the most active physical gold markets in the world. Spot gold can be traded through two closely related yet independent markets in the city — the Chinese Gold and Silver Exchange Society and the loco London gold market. The Society, established in 1910, provides trading of both tael bars and kilo bars[4]. Prices closely follow those in the other major gold markets in London, Zurich and New York.

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2 Mainland enterprises include H share companies, red-chip companies and non-H share Mainland private enterprises.

3 Corporations with the right to trade on or through the Stock Exchange and licensed under the Securities and Futures Ordinance to engage in such activity. Non-trading Stock Exchange Participants are not included.

4 Tael bars are of 99 per cent fineness and weighted in taels (one tael equals approximately 1.20337 troy ounces). Kilo bars are of 999.9 parts per thousand fineness and weighted in kilograms.

Hong Kong continues to be one of the most open insurance centres in the world. Among the 171 authorised insurers at year's end, 82 were from 20 overseas countries or the Mainland. Fourteen of the world's top 20 insurers are authorised to conduct insurance business in Hong Kong either directly or through a group company. There were 19 professional reinsurers in Hong Kong, including most of the world's top reinsurers. Gross premium income in 2009 was $185.7* billion.

The Government, including the Hong Kong Monetary Authority (HKMA) in particular, seeks to foster a better understanding of Hong Kong's economic and financial strengths among international credit rating agencies. In November 2009, Moody's upgraded the outlook for Hong Kong's local and foreign-currency ratings from 'Stable' to 'Positive', reflecting recognition of Hong Kong's credit strengths, particularly its strong external asset position and healthy public finances.

Major Achievements in 2009

Continued efforts were made in 2009 to enhance Hong Kong's competitiveness as an international financial centre in general and develop Hong Kong as a capital formation centre, asset management centre and offshore RMB business centre in particular, as pledged in the Chief Executive's October 2009 Policy Address. The Government continues to work closely with regulators and the industry to optimise Kong Kong's regulatory framework. It also continues to press ahead with various initiatives to develop further Hong Kong's fund-raising, wealth management and RMB business.

Enhancing Hong Kong's Competitiveness as a World Financial Centre

To build on Hong Kong's strength as an international financial centre, the Government optimises its regulatory framework to keep abreast of local and international developments, to enhance the quality of its markets and to increase their depth and breadth.

Optimising the Regulatory Framework

An effective regulatory regime is a pre-requisite to maintaining investor confidence and Hong Kong's standing as an international financial centre. During the year, the Government, the Hong Kong Monetary Authority and the Securities and Futures Commission implemented measures to better regulate the securities business conducted by banks and to strengthen investor protection. The HKMA took steps to require banks to attach 'health warnings' to retail derivative products, to audio-record the sales process of investment products and to separate clearly general banking business from securities-related activities. The SFC also launched a public consultation on the need for products' key facts statements, introduction of cooling-off periods, disclosure of commissions and fees and other relevant initiatives.

Hong Kong's financial system emerged from the global financial crisis without systemic problems, thanks to its robust regulatory regime. The financial tsunami

* Provisional statistics

prompted the G-20 countries and international regulatory bodies to propose a series of measures to better regulate financial institutions and markets. Hong Kong took part in the international discussions on the subject.

Expanding the Sources of Listed Enterprises on the Stock Exchange

Fund-raising Centre

Hong Kong is the premier capital formation centre for the Mainland whose enterprises have raised $2,489.9 billion since January 1993. The Hong Kong Exchanges and Clearing Limited (HKEx) has been stepping up its promotion of Hong Kong as a preferred listing venue as well as establishing closer co-operation with other stock markets.

In 2009, the HKEx's Listing Committee accepted in principle a number of new jurisdictions for overseas companies seeking listings on the SEHK. At December 2009, 10 jurisdictions – Australia, British Virgin Islands, Canada (British Columbia), Canada (Ontario), Cyprus, Germany, Jersey, Luxembourg, Singapore and the United Kingdom – had been accepted for this purpose, in addition to four jurisdictions recognised under the Listing Rules of Hong Kong, the mainland of China, Bermuda and the Cayman Islands. At year's end, over 100 overseas companies had been listed on the SEHK. HKEx will continue to admit new jurisdictions of an issuer's incorporation. HKEx members pay regular visits to the Mainland, Vietnam, Thailand, Malaysia, Kazakhstan, Russia, Taiwan and other places to promote Hong Kong as a premier capital formation centre.

Offshore RMB Business Centre

Hong Kong continued in 2009 to strengthen its position as the testing ground for liberalising the Mainland's capital account and regionalising as well as internationalising the RMB, and building a market to offer a broad range of RMB products and services.

RMB business in Hong Kong has developed in a steady and orderly manner. At the end of 2009, the outstanding RMB deposits in Hong Kong exceeded RMB 63 billion. Six RMB bond issues were made in 2009, including sovereign bonds worth RMB 6 billion issued by the Central People's Government's Ministry of Finance, bringing to RMB 38 billion the total amount of outstanding RMB bonds issued in Hong Kong.

An RMB trade settlement pilot scheme commenced operation in July 2009. Under it, cross-border trade transactions between certain cities in the Mainland, including Shanghai, Guangzhou, Shenzhen, Zhuhai and Dongguan, and Hong Kong, Macao, and ASEAN countries are eligible for settlement in RMB. Relevant Mainland authorities have published the list of pilot enterprises and arrangements for export tax rebate.

In 2009, improvements were made to the HKEx's Central Clearing and Settlement System and its ties to the interbank clearing system, to support the listing and trading of RMB-denominated products on the SEHK.

Asset Management Centre

China's strong economic rebound spearheaded Asia's overall economic recovery and created investment opportunities in the region in the wake of the financial tsunami. Hong Kong with its strong asset management foundation and world-class financial infrastructure is benefiting greatly from the huge demand for wealth and asset management services in the Mainland. Hong Kong is also well placed to become Asia's premier asset management centre.

The city's combined fund management business amounted to US$750 billion at the end of 2008, over 64 per cent of which was sourced from non-Hong Kong investors, underlining the city's strong appeal to foreign investment capital. At the end of December, there were 86 approved fund management groups managing 1 955 unit trusts and mutual funds authorised by the SFC.

During the year, the Government continued to lead financial services delegations to the Mainland and different countries to promote Hong Kong's financial services and its advantages as a major asset management centre in Asia.

Developing Islamic Finance

The Government is also pressing ahead with creating a conducive platform for developing Islamic finance in Hong Kong. After amending the relevant laws, tax neutrality arrangements will be put in place for the issue and transaction of common types of Islamic bonds vis-à-vis their conventional counterparts.

In November, the SFC signed a Declaration on Mutual Co-operation on Development of Islamic Capital Market and Islamic Collective Investments Schemes (the Declaration) with the Securities Commission Malaysia. The Declaration provides a framework for mutual recognition of Islamic collective investment schemes by Malaysia and Hong Kong, which is an impetus for developing further Islamic finance in Hong Kong.

Improvemens to the Mandatory Provident Fund Schemes Ordinance

Since the enactment of the Mandatory Provident Fund Schemes Ordinance in August 1995, the Mandatory Provident Fund Schemes Authority (MPFA) has been reviewing and making proposals to improve the Mandatory Provident Fund (MPF) legislation based on operational experiences. The amendments have simplified the running of MPF scheme, strengthened protection for scheme members and improved regulation of the schemes and their investments. On July 9, the Legislative Council passed the Mandatory Provident Fund Schemes (Amendment) Bill 2009 to allow employees to transfer in a lump-sum accrued benefits derived from their mandatory contributions made during their current employment from a contribution account to another MPF scheme of their choice at least once a year.

The new law lightens the portability restrictions on employees' mandatory contributions and gives them access to a broader spectrum of MPF service providers, MPF schemes for investing mandatory contribution funds. About 60 per cent of MPF benefits are expected to become portable after implementation of the new law, creating stronger competition in the market and encouraging more active management of MPF investments by employees.

Modernising the Companies Ordinance and other Legislative Amendments

The Standing Committee on Company Law Reform (SCCLR) advises the Government on reviews and reforms of Hong Kong's company laws and on enhancing corporate governance. Many of the legislative amendments recommended by the SCCLR have been adopted over the years.

The draft Companies Bill, which aims to enhance further Hong Kong's status as a major international business and financial centre, is undergoing public consultation in two phases.

Review of the Trustee Ordinance

The Government completed its consultation on a Trustee Ordinance review in September 2009. Legislative amendments will be introduced to provide a better framework for the operation of trusts in Hong Kong, strengthen the competitiveness of Hong Kong's trust services industry and enhance Hong Kong's position as a major asset management centre.

Enhancement of the Financial Infrastructure

Hong Kong has a robust Real Time Gross Settlement (RTGS) interbank payment system. All banks in Hong Kong maintain settlement accounts with the HKMA through the Hong Kong dollar RTGS system. All RTGS payment transactions are settled in real time. The banks may obtain intraday liquidity through intraday repurchase agreements with the HKMA using the Exchange Fund Bills and Notes (EFBNs) as collateral.

US dollar, Euro and Renminbi RTGS systems also enable transactions in these currencies to be settled in real time, reducing or eliminating settlement risk. RTGS systems in Hong Kong are linked to enable foreign-exchange transactions to be settled on a payment-versus-payment (PvP) basis.

The HKMA operates the Central Money markets Unit (CMU) to provide clearing and custodian services for EFBNs and other Hong Kong dollar or foreign-currency private debt securities. It is linked to a number of international and regional central securities depositories to enable overseas investors to trade CMU securities.

Through its integration with the RTGS systems, the CMU enables securities to be settled on a delivery-versus-payment (DvP) basis, enhancing settlement efficiency and eliminating settlement risk. The interface also enables users of RTGS systems to access intraday liquidity through automatic intraday repurchase agreements.

The Government, regulators, and the HKEx are committed to ensuring a safe and efficient financial infrastructure in Hong Kong. For example, the HKMA is devoted to providing a multi-currency, multi-dimensional platform. It is also developing Hong Kong as a payment and settlement centre in the region.

Major projects completed in 2009 include:

- Phase I of SWIFTNet migration[5];
- Extension of operation of foreign-currency RTGS systems and the CMU to include all Hong Kong general holidays except January 1; and
- Establishment of multi-currency cross-border payment arrangements between the Mainland and Hong Kong.

A working group comprising representatives of the SFC, HKEx and the Federation of Share Registrars Limited, issued a joint consultation paper in December 2009 seeking public views on a proposed operational model for implementing a scripless securities market in Hong Kong. To underline its support for this initiative and to lay the foundation for the setting up of a scripless securities market in Hong Kong, the Government has proposed, as a first step, technical amendments to the Companies Ordinance to remove legal obstructions to scripless securities holding and trading. This would help the market better concentrate on the discussions on the proposed operational model for implementing a scripless securities market.

Development of the Bond Market

The Government has boosted development of the bond market in recent years by providing it with the necessary financial infrastructure, simplifying the issuance process, optimising regulatory arrangements, offering tax incentives, encouraging public corporations to issue bonds and strengthening education for bond investors.

To promote development of the local bond market, the Government obtained the Legislative Council's approval in July 2009 to implement the Government Bond Programme (GBP), under which the Government is authorised to issue bonds with an aggregate outstanding principal of up to HK$100 billion and to set up the Bond Fund to manage the sums raised under the GBP. The Bond Fund is not treated as part of the fiscal reserves and is managed separately from other Government accounts. It is used to repay principal, meet the financial obligations and liabilities associated with the GBP and make investments.

The GBP comprises the institutional bond issuance and the retail bond issuance programmes. In 2009, two tranches of Government bonds for institutional investors were issued, attracting a diverse group of investors.

With ample liquidity in the interbank market, banks' demand for short-dated Exchange Fund papers for liquidity management increased substantially. In response to strong demand, the HKMA issued an additional HK$374.4 billion worth of Exchange Fund Bills in 2009. It also continued fine-tuning the maturity mix of EFBNs with increased issuance of 5-, 10- and 15-year Exchange Fund Notes.

Outstanding Hong Kong dollar debts, including EFBNs, exceeded HK$1,111 billion at the end of 2009. During the year, HK$1,048 billion worth of EFBNs and HK$194 billion worth of other Hong Kong dollar debts notes were issued.

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5 It replaces the closed, proprietary platform of Hong Kong's RTGS systems and the CMU with an open platform using Internet technology.

Development of a Secondary Mortgage Market

A well-developed secondary mortgage market is useful in channelling long-term funds, such as insurance and pension funds, to meet demand for long-term home financing. The Hong Kong Mortgage Corporation (HKMC) was set up in March 1997 to carry out the following tasks:

- Enhance the banking sector's stability by offering a reliable source of liquidity, thereby reducing the banks' concentration of risk exposure to mortgages and associated liquidity risks;
- Promote wider home ownership; and
- Facilitate the growth and development of the debt securities and mortgage-backed securities markets in Hong Kong.

Asset Purchase Programme

Under the Asset Purchase Programme, the HKMC purchases assets from financial institutions to facilitate their risk and balance sheet management. The HKMC's local asset portfolio had an outstanding principal balance of $28.3 billion at the end of 2009.

Mortgage Insurance Programme

The Mortgage Insurance Programme (MIP) was launched in 1999 to provide mortgage insurance cover to banks enabling them to extend residential mortgage loans to homebuyers above the 70 per cent loan-to-value ceiling set by the HKMA.

The MIP has gained wide acceptance and has promoted home ownership through product diversification and improvements to servicing standards. Over 37 000 applications for mortgage loans amounting to $89 billion were approved in 2009.

Debt Issuance

The HKMC plays an important role in promoting the Hong Kong dollar debt market's development. By the end of 2009, it had $44.5 billion of debt securities outstanding with a tenure of up to 15 years. The HKMC pioneered the development of Hong Kong's retail bond market in 2001, with a total issuance of HK$13.7 billion, of which $1.9 billion was outstanding at the end of 2009.

Mortgage-backed Securities Market

The HKMC has a back-to-back mortgage-backed securities (MBS) programme that provides a platform for banks to repackage effectively their mortgage portfolios into more liquid MBS. A total of $1.9 billion of MBS were outstanding under this programme at year-end.

Upgrading of the Quality of Financial Reporting

The Government continues to press ahead with the enhancement of market quality and investor protection in collaboration with stakeholders, including the Financial Reporting Council (FRC), a statutory body established to investigate Hong Kong listed companies' audit irregularities and non-compliance with accounting standards. The FRC started reviewing in July 2008 modified auditor's reports of financial statements of entities listed in Hong Kong.

Statistics on FRC's work

	2007	**2008**	**2009**
No. of complaints received	17	12	13
No. of modified auditors' reports reviewed	Not applicable	28	129
No. of investigations initiated	1	-	4
No. of investigations completed	-	1	-
No. of enquiries initiated	1	1	2
No. of enquiries completed	-	1	2

A Process Review Panel reviews the FRC's handling of cases to ensure its actions and decisions comply consistently with established procedures.

Proposed Establishment of an Independent Insurance Authority

The Government has been looking into the establishment of an independent Insurance Authority (IA) to enable it to operate more flexibly to meet regulatory challenges and to better prepare Hong Kong for a risk-based capital regulatory regime.

In view of the latest development in the financial market, the Government carried out an extended study in late 2009 to review the existing insurance regulatory system and identify areas for improvement. The study is expected to be completed in the second quarter of 2010. The Government will prepare the detailed proposals for public consultation in mid-2010.

Proposed Establishment of a Policyholders' Protection Fund

To improve the stability of the insurance market and safeguard the interests of policyholders in the event of an insurer's insolvency, the Government has proposed the establishment of a Policyholders' Protection Fund (PPF) in Hong Kong and aims to consult the public on the detailed proposals of PPF in 2010.

Review of proposals for introducing a corporate rescue procedure

As part of its response to the global financial crisis, the Government has adopted the recommendation made by the Task Force on Economic Challenges in January 2009 to re-consider the introduction of a corporate rescue procedure to help companies with viable long-term business prospects, in short-term financial difficulty, to turn around.

The Government launched a three-month public consultation on the subject in October 2009.

Anti-Money Laundering and Counter Financing of Terrorism

Hong Kong watches closely its anti-money laundering (AML) and counter financing of terrorism (CFT) programme to maintain a safe business and investment environment. A high-level Central Co-ordinating Committee on AML and CFT, chaired by the Financial Secretary, is in place to give steer on this policy area.

Financial Links with the Mainland

Strengthening financial co-operation with the Mainland is one of Hong Kong's key strategies in enhancing its competitiveness as an international financial centre. The Government continues to seize the opportunities presented in the 'one country, two systems' principle to promote Hong Kong's financial services.

The Government endeavours to meet the Mainland's overall development needs and to contribute to its prosperity and financial security by:

(1) Building on Hong Kong's strength as an international market and enhancing the quality and competitiveness of its market to attract international talent, capital, financial institutions and products;

(2) Strengthening Hong Kong's position as a testing ground for liberalising the Mainland's capital account and regionalising and internationalising the RMB, and building a market capable of offering a broad range of RMB products and services;

(3) Leveraging on pilot measures to improve a two-way flow of financial products, capital and talent between Hong Kong and the Pearl River Delta region and to set up financial institutions in both places;

(4) Serving as the preferred capital-raising centre for Mainland enterprises operating outside the Mainland, providing equity listing, bond issuance, international asset management and hedging services. In this regard, Hong Kong can act as the bridgehead for Mainland entrprises to enter the international market; and

(5) Strengthening the links between Mainland and Hong Kong financial markets in the areas of market infrastructure, information sharing, and regulatory co-operation to reinforce security of cross-border capital flows.

In December 2009, Premier Wen Jiabao pledged the nation's support for consolidating Hong Kong's role as a testing ground for launching the country's financial reforms. Specifically, he endorsed further development of the following initiatives:

- RMB business, including cross-boundary trade settlement;
- RMB financing and direct investment;
- RMB bond business;

- Listing of Mainland enterprises in Hong Kong; and
- Co-operation between Shanghai and Hong Kong capital markets.

There has been a steady flow of funds between financial institutions on both sides of the boundary. Over the years, the Mainland has accumulated a substantial amount of funds in Hong Kong dollars from trading activities and inward investment. These funds are placed with financial institutions in the Mainland and are subsequently channelled back to Hong Kong through the inter-bank market.

By the end of 2009, AIs' external liabilities to banks in the Mainland amounted to $318.9 billion, while their claims on banks in the Mainland totalled $379 billion. These sums represent 12.7 per cent and 8.3 per cent respectively of AIs' total liabilities to and claims on banks outside Hong Kong.

The Mainland's budding fund management industry has prompted Hong Kong-based fund managers to form joint ventures with their Mainland counterparts. Hong Kong fund managers have also paved the way for investors to seize investment opportunities in the Mainland. At year-end, there were 29 SFC-authorised funds with significant exposure to A-shares via the fund managers' own Qualified Foreign Institutional Investment (QFII[6]) quota and six Exchange-traded Funds (ETFs) that tracks the A-share market, as well as funds that invest indirectly in A-shares via equity-linked investments issued by qualified foreign institutional investors, and guaranteed funds with their upside potential returns linked to A-share market performance.

Capital Formation Centre and Global Investment Platform for the Mainland

Hong Kong's fundamental strengths, enhanced by its high market liquidity, a robust regulatory system, efficient information flow, a rich pool of financial professionals and proximity to the Mainland market, make it an ideal provider of top class services to Mainland enterprises seeking listing in the city, widely known as international financial centre.

The growing presence of Mainland issuers in Hong Kong has increased the breadth and depth of Hong Kong's securities and futures markets. Hong Kong's equity market has evolved from one with a high concentration of property and financial businesses to one with a great diversity of constituent stocks and a wide range of products.

Mainland enterprises also raise capital in Hong Kong through the issuance of bonds, project financing and loan syndication. In addition, they have easy access to investment banking services for mergers and acquisitions, and consultancy on restructuring.

6 Foreign institutions approved by the China Securities Regulatory Commission as Qualified Foreign Institutional Investors (QFIIs) may invest in China A shares and other RMB-denominated securities in the Mainland subject to the grant of investment quotas by State Administration of Foreign Exchange.

The HKEx signed Closer Co-operation Agreements with its counterparts in Shanghai and Shenzhen in January and April respectively. The accords commit the three bourses to work closely to achieve their common goal of meeting the domestic and international fund-raising needs of Chinese enterprises to enable them to continue contributing to China's greater economic development.

In August, the SEHK consulted the Hong Kong market on the acceptance of Mainland accounting and auditing standards and auditors for Mainland-incorporated companies listed in Hong Kong. The proposal was made jointly by Hong Kong and Mainland regulators. This would mean more timely disclosure of information to investors and increased market efficiency. It would also reduce compliance costs for Mainland incorporated issuers.

Mainland and Hong Kong Closer Economic Partnership Arrangement

The Closer Economic Partnership Arrangement (CEPA) between the Mainland and Hong Kong which went into force in 2004, gives Hong Kong's financial services suppliers and professionals greater market access and flexibility for their operations in the Mainland. It has also enhanced Hong Kong's attractiveness to market users and strengthened the city's competitiveness as an international financial centre and the premier capital formation centre for Mainland enterprises.

Supplement VI to CEPA was announced on May 9, 2009. To strengthen further co-operation between the Mainland and Hong Kong in the securities sector, it was agreed that the Mainland shall allow qualified Mainland securities companies, approved by the China Securities Regulatory Commission, to set up subsidiaries in Hong Kong in accordance with the relevant requirements.

A further major breakthrough introduced under Supplement VI allows Hong Kong and Mainland securities companies to set up joint venture securities investment advisory companies (JV firms) in Guangdong. (The JV firm shall be a subsidiary of the Mainland securities company while the Hong Kong company's shareholding in the JV must not exceed one-third of the JV company's total shareholding). Supplement VI also allows both sides to study the introduction of open-ended index-tracking ETFs, the portfolios of which are constituted in Hong Kong listed stocks, in the Mainland.

A new measure for the banking sector under Supplement VI came into effect on October 1, 2009, allowing Hong Kong banks, through their branches or wholly owned subsidiaries in the Mainland to set up 'cross-location' sub-branches in Guangdong, but outside the municipality where the original branch is situated. The measure enables Hong Kong banks to expand their branch networks in Guangdong in a more cost-effective way.

The accounting sector also benefits from Supplement VI which enables Hong Kong residents who have formally become members of the Hong Kong Institute of Certified Public Accountants (HKICPA) on or before March 31, 2009 to be exempted from taking the test on Finance and Accounting in the Mainland's Certified Tax Agent qualification examination.

Shanghai-Hong Kong Financial Co-operation

China's State Council announced in March 2009 that, Shanghai will become an international financial centre by 2020 in line with China's economic strength and the international status of its currency, the RMB. The announcement also calls for a strengthening of co-operation between Shanghai and Hong Kong in the development of Shanghai's financial centre.

It is to China's advantage to have two financial systems working side by side. Hong Kong will work with Shanghai to strengthen the development of both cities' securities and bond markets, encourage mutual establishment of financial institutions, and train and exchange financial talents.

Guangdong-Hong Kong Financial Co-operation

Guangdong is the Mainland province closest to Hong Kong in geographical, cultural and economic terms. Guangdong and Hong Kong are continually looking into ways of strengthening further financial co-operation with each other. The Central People's Government has endorsed the approach of leveraging the pilot measures stipulated in 'The Outline of the Plan for the Reform and Development of the Pearl River Delta', which is designed to further enhance co-operation between the Pearl River Delta region and Hong Kong and Macao.

An expert group was set up in August under the Hong Kong-Guangdong Co-operation Joint Conference to discuss closer co-operation between the two places in conducting their securities, banking, RMB and insurance businesses.

Banking Sector

Main Features

Hong Kong maintains three tiers of deposit-taking institutions, comprising licensed banks, restricted licence banks and deposit-taking companies. They are known collectively as Authorised Institutions (AIs) under the Banking Ordinance. The HKMA is the licensing authority for AIs.

Only licensed banks may conduct full banking services, including in particular the provision of current and savings accounts and acceptance of deposits of any size and maturity. Restricted licence banks may take deposits of any maturity of $500,000 or above. Deposit-taking companies may take deposits of $100,000 or above with an original maturity of at least three months.

Hong Kong has one of the highest concentrations of banking institutions in the world. At the end of 2009, there were 145 licensed banks, 26 restricted licence banks and 28 deposit-taking companies. These 199 AIs maintained a network of more than 1 300 local branches. There were also 71 representative offices of overseas banks in Hong Kong at year's end.

The total deposit liabilities of all AIs to customers and the total loans and advances extended by these institutions at the end of 2009 were $6,381 billion and $3,289 billion respectively. The total assets of all AIs amounted to $10,661 billion.

Hong Kong Monetary Authority

The HKMA was established on April 1, 1993 after the Legislative Council passed amendments to the Exchange Fund Ordinance in 1992 empowering the Financial Secretary to appoint a Monetary Authority.

Its policy objectives are to maintain currency stability within the framework of the Linked Exchange Rate system through sound management of the Exchange Fund, monetary policy operations and other means deemed necessary; promote safety and stability of the banking system through the regulation of banking business, the business of taking deposits and the supervision of AIs and promote efficiency, integrity and development of the financial system, particularly payment and settlement arrangements.

The HKMA is an integral part of the Government, but can employ staff on terms that differ from those of the civil service to attract personnel of the appropriate experience and expertise. Its staff and operating costs are charged directly to the Exchange Fund instead of the general revenue. The HKMA is accountable to the Financial Secretary, who is advised by the Exchange Fund Advisory Committee (EFAC) on investment policies and strategies for the Exchange Fund and on projects that are charged to the Exchange Fund, such as the development of financial infrastructure.

The Banking Advisory Committee and the Deposit-taking Companies Advisory Committee are established under the Banking Ordinance to give advice on relevant policy matters. They are chaired by the Financial Secretary and comprise members from the banking industry and other professions.

The Banking Ordinance provides the legal framework for banking supervision in Hong Kong. Under the ordinance, the HKMA is the licensing authority responsible for granting and revoking the authorisation of all AIs, and the approval and revocation of money broker licences. The HKMA seeks to maintain a regulatory framework that is fully in line with international standards. The aim is to devise a prudential supervisory system to help preserve the general stability and effective operation of the banking system, while at the same time providing sufficient flexibility for AIs to make commercial decisions.

Hong Kong's framework of banking supervision is in line with the Core Principles for Effective Banking Supervision issued by the Basel Committee on Banking Supervision. In June 2009, at the invitation of the Basel Committee, Hong Kong became one of its members. The HKMA also participates in a number of international and regional initiatives and forums for banking supervisors.

Recent Developments

Hong Kong's banking sector managed to weather the challenges of the global financial crisis, ending the year with sound capital and liquidity positions. Further steps were taken by the HKMA to implement international initiatives to strengthen banks' capital, liquidity and other risk management standards; and AIs introduced improved measures on investor protection.

The SFC, the HKMA and a number of banks reached an agreement in relation to the repurchase of Lehman Brothers Minibonds from eligible customers in July 2009.

In 2009, the HKMA continued to deploy a large amount of resources to investigate complaints concerning Lehman Brothers-related financial products. Taking into account the cases that had been dealt with through the repurchase agreements reached among the SFC, the HKMA and the banks in 2009, the HKMA is expected substantially to complete all the cases by end of March 2010.

Assisted by the HKMA, the Hong Kong Deposit Protection Board (HKDPB) completed a two-phase review of the Deposit Protection Scheme and the public consultations on the recommendations arising from the review. The Government, in collaboration with the HKDPB, started drafting legislative amendments for effecting the recommendations and it aims to implement them upon the expiry of the full deposit guarantee which is scheduled to expire at the end of 2010.

Securities and Futures Sector

Main Features

The securities market in Hong Kong is operated by the SEHK and futures market, the Hong Kong Futures Exchange Limited (HKFE), both being wholly owned subsidiaries of the HKEx.

By the end of 2009, there were 1 319 companies listed on the Main Board and the Growth Enterprises Market (GEM) of the SEHK with a total market capitalisation of about $17,874 billion, raising an aggregate of $642.1 billion within the year. The total turnover of the securities market amounted to $15,515 billion.

The structured product market continued to expand in 2009. At the end of December 2009, Hong Kong was the second largest market of ETFs in Asia in terms of both turnover and market capitalisation. During the year, 19 new ETFs were authorised, increasing the total number of ETFs listed on the SEHK to 43, offering a wide range of investment exposures to world, regional and Mainland indices and commodities for investors. Turnover of ETFs reached a record high of $499.7 billion compared with the previous record of $411.1 billion set in 2008. The SFC entered into a mutual recognition arrangement with the Taiwan Financial Supervisory Commission in May 2009 to facilitate cross-listing of ETFs. So far, three Hong Kong ETFs were cross-listed in Taiwan and one Taiwan ETF was cross-listed in Hong Kong.

The number of newly listed Callable Bull/Bear Contracts (CBBCs) set a new record which increased to 8 072 in 2009 from 4 231 in 2008. At the end of 2009, there were 1 692 CBBCs listed in Hong Kong. Turnover of CBBCs increased from $1,039.6 billion in 2008 to $1,676.1 billion in 2009. There were a total of 3 367 derivative warrants listed on the securities market at the end of 2009. Turnover of derivative warrants was $1,655 billion during the year. Stock options turnover decreased from 54 692 865 contracts in 2008 to 47 439 896 contracts in 2009.

In the derivatives market, there were some new records. Turnover of Mini Hang Seng Index Futures and options recorded turnover of 9 279 877 contracts and 286 591 contracts respectively, rising 17 per cent and 83 per cent from 2008. Turnover of H-shares Index options was 1 961 131 contracts, the highest ever. There was also record high open interest for Mini Hang Seng Index futures and options and H-shares Index options.

In the futures market, around 99 million futures and options contracts were traded in 2009, slightly lower — by 6 per cent — than in 2008. The Hang Seng Index Futures and the H-shares Index Futures recorded a turnover of 20 728 034 contracts and 12 394 116 contracts respectively, falling 5 per cent and 14 per cent from 2008.

At year end of 2009, there were 13 automated trading services providers, comprising mainly foreign exchanges and regulated entities, authorised by the SFC to provide automated trading services in Hong Kong. Automated trading services are services provided by means of electronic facilities, not being facilities provided by a recognised exchange company or a recognised clearing house, to transact or settle transactions in securities or futures contracts.

Securities and Futures Commission

The SFC was established in May 1989 following the enactment of the Securities and Futures Commission Ordinance, which was replaced by the Securities and Futures Ordinance (SFO) that came into effect on April 1, 2003. Established as an autonomous statutory body, the SFC is responsible for regulating the securities and futures markets in Hong Kong. The SFC has a governing body of 14 directors appointed by the Chief Executive. The Government is not involved in the day-to-day regulation of the securities and futures industry.

The SFC is funded by the market. No government funding has been sought since 1993. Its total expenditure in 2009-10 is estimated to be $793 million.

The exercise of powers by the SFC is subject to a range of checks and balances. For instance, a wide range of SFC decisions are subject to appeal at the independent Securities and Futures Appeals Tribunal. The Process Review Panel for the SFC (PRP) was established in 2000 to review and advise the SFC on the adequacy of the internal procedures and operational guidelines governing the actions and operational decisions it takes in the performance of its regulatory functions. The PRP's eighth annual report, which was published in September 2009, concluded that the SFC had generally followed its internal procedures in handling cases under review.

Broadly speaking, the SFC's work involves licensing, supervision and monitoring of intermediaries; regulation of the public marketing of collective investment schemes, e.g. mutual funds; regulation of takeovers, mergers and other corporate activities; listing regulation under the dual filing system for IPO applicants and issuers; supervision of markets including the exchanges and clearing houses; enforcement of securities laws and rules; and investor education.

At end 2009, there were 35 935 licensed persons, including securities brokerage firms, futures dealers and securities margin financiers, as well as their representatives, and 107 registered institutions, such as banks, engaging in regulated activities like dealing and advising on securities and futures.

Market Misconduct

Market misconduct is subject to criminal prosecution or civil proceedings. The first conviction leading to jail sentences for insider dealing took place in 2009. Ten individuals were convicted of insider dealing in the indictable trials for this offence under the SFO, including a former managing director of a global bank who was jailed for seven years and fined $23 million, a record high imposed on an insider. The first indictable prosecution for market manipulation under the SFO also happened during the year. Separately, the SFC also maintained civil proceedings to secure the suspected proceeds of market misconduct. In one case the SFC secured interim orders freezing assets generated from a suspected fraud of up to HK$1.655 billion, the largest amount that the SFC had ever applied to the Court to freeze.

The Market Misconduct Tribunal (MMT), established in 2003, carries out civil proceedings and hears cases referred to it by the Financial Secretary following investigation by the SFC. In 2009, the MMT concluded three cases, and nine persons or companies were found to have engaged in market misconduct. The MMT's predecessor, the Insider Dealing Tribunal (IDT), finalised its last two cases, bringing the number of cases concluded by the IDT to 27 and finding 65 persons culpable of insider dealing.

Recent Developments

Investor protection and education continued to be the highlight of the post-crisis year.

In April 2009, the SFC for the first time intervened in the privatisation proceedings commenced by a large telecommunications company in the interest of minority shareholders. Upon gathering evidence at the shareholders' meeting and studying circumstances surrounding share transfers of single board lots before the meeting, the SFC applied to the court to sanction the delisting scheme. The court ruled in favour of the SFC, saying that share splitting for the purpose of manipulating the outcome in a scheme of arrangement is a form of abuse.

The collapse of Lehman Brothers in September 2008 triggered complaints about sales of structured investment products by financial intermediaries to retail investors. To resolve the complaints efficiently and effectively, the SFC adopted a 'top-down' approach, examining, among other aspects, systemic problems with product marketing, including the selling practices and internal controls of intermediaries. In January 2009, a major local brokerage reached an agreement with the SFC to repurchase Lehman Minibonds from eligible clients in full. This set the stage for resolution with other Lehman Minibond distributors. In July, the HKMA and SFC struck an agreement with 16 distributing banks to repurchase from about 25 000 eligible clients the Lehman Minibonds at 60 per cent or 70 per cent of their original investment value, with the higher percentage going to those 65 and older.

In the area of investor education, a number of initiatives were launched using the theme 'Be Smart, Ask First'. For the first time, a year-long, multi-media advertising campaign was conducted. This was kicked off by TV and radio commercials featuring a catchy remake of a Canto-pop song *'Ask Me'*. It involved a series of initiatives, including a photo competition, a financial knowledge competition and an investment story competition, as well as outreach activities such as university courses and talks to the elderly and young people.

In addition to its investor education website, the SFC continued its use of the mass media and interactive approaches to disseminate its investor educational messages. During the year, TV, radio, videos on buses, free newspapers, notices on public transport, and poster displays at MTR stations and bus shelters were used to convey educational messages to the community. A TV game show and an 'infommercial' series broadcast highlighting investment knowledge, an understanding of risks and proper investment attitudes.

Insurance Sector

Main Features

At year-end, there were 171 authorised insurers, 89 of which were incorporated in Hong Kong while the remaining 82 were incorporated in the Mainland and in 20 overseas countries, with Bermuda taking the lead.

During the past five years, the Hong Kong insurance industry achieved an average annual growth of 8.9 per cent. The total gross premiums of the insurance industry reached $185.7* billion in 2009, representing a 1.6 per cent decrease over 2008.

Gross premiums of the general insurance sector increased by 7.1 per cent to $28.6* billion in 2009.

The increase was primarily boosted by accident and health business (comprising medical business). On the other hand, overall underwriting profit of general insurance business grew from a profit of $1.3 billion to $2.2* billion in 2009, attributable to improvement in claims experience.

The total revenue premiums of long-term insurance business dropped 3 per cent to $157.1* billion in 2009. The individual life business remained dominant with the premiums in force of $128.8* billion, accounting for 82 per cent of the total revenue premiums. The number of individual life policies in force grew by 5.3 per cent to 8.6* million in 2009.

* Provisional statistics

At year-end, there were 34 991 insurance intermediaries, including 34 429 agents of whom 2 327 were agency firms and 562 brokers.

Insurance Authority

The Commissioner of Insurance, appointed by the Chief Executive as the Insurance Authority (IA), has the principal function under the Insurance Companies Ordinance (ICO) to regulate and supervise the insurance industry to promote its general stability and protect policy holders.

The ICO prescribes a regulatory framework for all classes of insurance business to ensure the financial stability of all insurers authorised in Hong Kong and the fitness and propriety of their management. The IA may take appropriate actions under the ICO against an insurer to safeguard the interests of policyholders.

The ICO also sets out the self-regulatory framework for insurance intermediaries. The self-regulatory organisations include the Insurance Agents Registration Board under The Hong Kong Federation of Insurers, the Hong Kong Confederation of Insurance Brokers and the Professional Insurance Brokers Association.

As a member of the International Association of Insurance Supervisors (IAIS), Hong Kong makes its best efforts to ensure that its supervisory regime is in line with prevailing principles and standards. It has also established an Insurance Advisory Committee to advise the Chief Executive on matters relating to the administration of the ICO and the carrying on of insurance business in Hong Kong.

Recent Developments

In view of the financial crisis, the IA with the support of a robust regulatory framework, has stepped up its monitoring of market movements and their impact on the financial and solvency position of authorised insurers in Hong Kong.

The global financial crisis has called for further strengthening of investor protection. In this regard, the IA and the insurance industry have worked together to enhance the disclosure and suitability assessment of investment-linked assurance scheme (ILAS) products so as to ensure that consumers purchase products that are suitable for them and consistent with their needs and risk appetite. These measures include an improved version of the Financial Needs Analysis, a Risk Profile Questionnaire, and a declaration by the insured that he fully understands the product features. Insurers are also required to make phone calls to vulnerable clients (i.e. clients who are (i) aged over 65; (ii) with education at primary level or below; or (iii) with no regular source of income) to confirm suitability assessment. To upgrade the professional knowledge of insurance intermediaries selling ILAS products, the IA enhanced the examination syllabus for the Investment-Linked Long Term Insurance Examination paper under the Insurance Intermediaries Qualifying Examination. It was planned that with effect from March 2010, all new insurance intermediaries wishing to sell ILAS would have to pass the revised examination paper. In addition, consumer education on ILAS products has been stepped up.

As a member of the IAIS, the IA contributes to the development of international standards in insurance supervision. The IAIS has been analysing the financial crisis and its impact on the global insurance in order to identify areas for reform, with particular emphasis on enhancing group and cross sectoral supervision. The IA will keep in view any new standards promulgated by the IAIS and consider adopting them in Hong Kong, taking into account local circumstances.

In addition, the IA will continue to participate in supervisory colleges so as to work closely with overseas regulators on regulating major insurance groups.

Mandatory Provident Fund Schemes and Occupational Retirement Schemes

Main Features

On December 1, 2000, the MPF System was implemented to help encourage the workforce to save and invest for their retirement. It is a privately managed, employment-related mandatory system of provident fund schemes. Unless exempted, employees and self-employed people aged between 18 and 65 are required to join MPF schemes.

The employer and employee are each required to contribute five per cent of the employee's relevant income to a registered MPF scheme, subject to the maximum and minimum levels of income for contribution purposes. The accrued benefits are fully vested in the scheme members and can be transferred when employees change employment or cease to be employed. A self-employed person has to contribute five per cent of his or her relevant income. In normal circumstances, benefits must be preserved until the scheme member attains the retirement age of 65. By end 2009, 99.9 per cent of employers (about 238 000), 99.9 per cent of relevant employees (2 209 000) and 75.5 per cent of self-employed persons (263 000) had participated in MPF schemes. Total MPF assets amounted to about $309 billion.

Unlike the compulsory MPF schemes, occupational retirement schemes registered under the Occupational Retirement Schemes Ordinance (ORSO) are voluntary schemes established by employers. To tie in with the implementation of the MPF system in 2000, schemes registered under the ORSO that fulfilled certain conditions were exempted from MPF requirements. Members of such schemes may choose to remain in the existing scheme or join an MPF scheme. At year-end, there were 4 440 MPF-exempted occupational retirement schemes covering over 400 000 employees.

Mandatory Provident Fund Schemes Authority (MPFA)

Established in September 1998 under the Mandatory Provident Fund Schemes Ordinance (MPFSO), the MPFA is responsible for regulating and supervising the MPF

System and ensuring compliance with the ordinance. It is also the Registrar of Occupational Retirement Schemes. To protect the interests of MPF scheme members, the MPFA closely monitors the operation of MPF trustees and other service providers, investigates cases of non-compliance identified through reports, complaints or proactive inspections, and takes enforcement actions accordingly. The MPFA also conducts MPF investment education to strengthen public awareness of the need to take care of their MPF investment and disseminates messages that will assist scheme members in choosing appropriate funds.

Recent Developments

The Government and the MPFA implemented the Financial Secretary's budgetary measure announced in the 2008-09 Budget to make a one-off injection of $6,000 into the account of each eligible MPF/ORSO scheme member who earned not more than $10,000 a month in order to enhance their retirement protection. By end-December 2009, over 1.4 million eligible persons received special injections amounted to over $8.4 billion.

As part of its continuing efforts to enhance the operation of the MPF system, the Government introduced the Mandatory Provident Fund Schemes (Amendment) Bill 2009 in May 2009. The Bill, which seeks to encourage more active management of MPF investments by employees and promote stronger market competition, was passed by the Legislative Council in July 2009. The MPFA is making preparations with MPF trustees to implement the legislation.

Companies Registry

The Companies Registry (the Registry) administers and enforces the major part of the Companies Ordinance (CO). The Registry registers local and non-Hong Kong companies and documents required to be filed under the CO and related ordinances, deregisters defunct solvent private companies and provides the public with services and facilities for inspecting and obtaining company information kept by the Registry. It administers and enforces several other ordinances including the Trustee Ordinance (insofar as it relates to trust companies), the Registered Trustees Incorporation Ordinance and the Limited Partnerships Ordinance. The Registry is also responsible for processing applications related to money lenders licences as well as maintaining a register of money lenders for inspection by members of the public.

The Registry has been operating as a trading fund department since 1993. Consequently, it can deploy its resources more flexibly to meet customers' demands and expectations. The department achieved a surplus of $134.7 million in 2008-09.

The Registry has continued to implement the Integrated Companies Registry Information System in phases to fully computerise its operations and enable electronic delivery of services in filing, processing, storing and providing company information. The electronic search services have been well received by customers and over 98 per cent of company searches are conducted online nowadays. Electronic services for company incorporation and a one-stop service for company incorporation and business registration are expected to be launched in 2010-11 pending the enactment of relevant legislative amendments.

In 2009, a total of 109 424 local companies were incorporated. By the end of 2009, 772 253 local companies were on the register, compared with 710 766 in 2008.

Companies incorporated outside Hong Kong must register with the Registry within one month of establishing a place of business in Hong Kong. During the year, 683 non-Hong Kong companies were registered and, by year-end, there were 7 912 registered non-Hong Kong companies from 81 countries.

Bankruptcies, Individual Voluntary Arrangement and Compulsory Winding-up

The Official Receiver (OR)'s Office ensures that service in personal and corporate insolvencies is of a high quality on a par with international standards.

When acting as the trustee or liquidator, the OR or a private sector insolvency practitioner investigates the affairs of the bankrupt or the wound-up company, realises assets and distributes dividends to creditors. The OR also prosecutes insolvency related offences under the Bankruptcy Ordinance and the CO, applies for disqualification orders against unfit company directors of wound-up companies, monitors the conduct of outside liquidators and trustees, and monitors the liquidation monies.

Chart 9 **Assets realised by the Official Receiver and dividends paid to creditors**

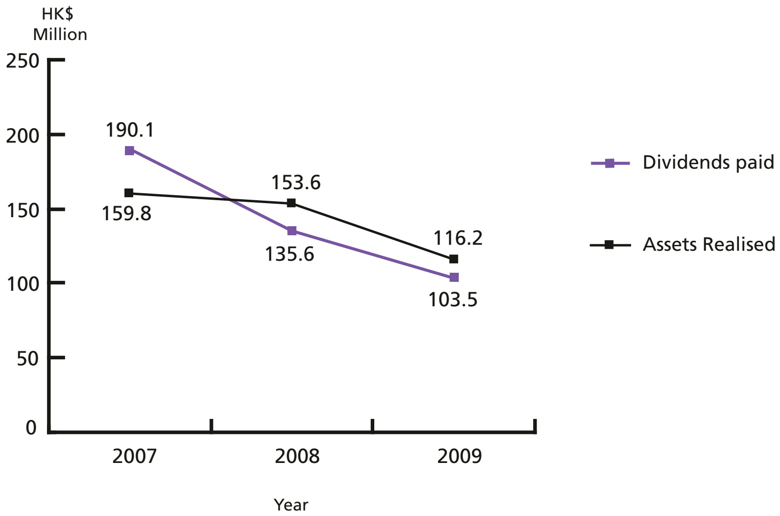
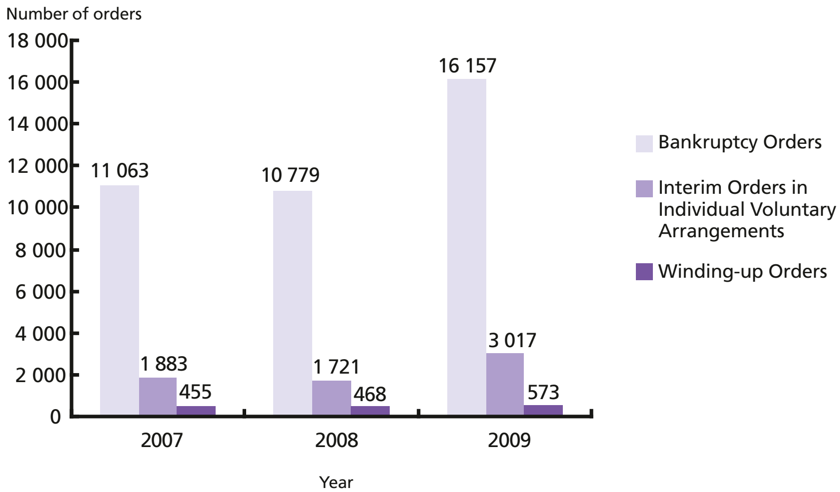


Chart 10 **Bankruptcy Orders, Interim Orders in Individual Voluntary Arrangements and Winding-up Orders made**



Professional Accountancy

The Hong Kong Institute of Certified Public Accountants (HKICPA) is established under the Professional Accountants Ordinance to perform a wide range of functions, such as registering certified public accountants (CPA); setting and maintaining financial reporting, auditing and ethical standards for the profession; and conducting training programmes and qualifying examinations.

Numbers of CPAs, CPA firms and corporate practices in Hong Kong:

	2007	2008	2009
No. of CPA, including CPA (Practising)	26 848	27 884	29 107
No. of CPA (Practising)	3 624	3 679	3 749
No. of firms of CPA (Practising)	1 172	1 176	1 198
No. of corporate practices	227	254	291

The Hong Kong Financial Reporting Standards (HKFRS), issued by the HKICPA, have converged with the International Financial Reporting Standards (IFRS). This convergence is beneficial to Hong Kong because international investors and financial analysts are well acquainted with IFRS.

Monetary Policy

The monetary policy objective of Hong Kong is currency stability, defined as a stable external exchange value of the currency of Hong Kong, in terms of its exchange rate in the foreign exchange market against the US dollar, at around

HK$7.80 to US$1. This clear policy aim is achieved through the linked exchange rate system introduced in 1983.

The linked exchange rate system is characterised by currency board arrangements requiring the Hong Kong dollar monetary base to be at least 100 per cent backed by — and changes in it to be 100 per cent matched by — corresponding changes in US dollar reserves held in the Exchange Fund at the fixed exchange rate of $7.80 to US$1. In Hong Kong, the monetary base includes the amount of currency notes and coins issued, the Aggregate Balance (the sum of the clearing balances of banks held with the HKMA for the purpose of effecting the clearing and settlement of transactions between banks themselves and also between the HKMA and banks), and the outstanding amount of EFBNs.

Banks have unrestricted access to a Discount Window for day-end liquidity through repurchase agreements using EFBNs as collateral. Under the currency board system, Hong Kong dollar exchange rate stability is maintained through an interest rate adjustment mechanism. The monetary base increases when the foreign currency (in Hong Kong's case, US dollars) to which the domestic currency is linked, is sold to the currency board for the domestic currency (inflow into the Hong Kong dollar). It contracts when the foreign currency is bought from the currency board (outflow from the Hong Kong dollar).

The expansion or contraction in the monetary base leads interest rates for the domestic currency to fall or rise, respectively, creating the monetary conditions that automatically counteract the original capital movements, ensuring stability of the exchange rate.

A Currency Board Sub-Committee under the EFAC was established in August 1998 to oversee the operation of the currency board system in Hong Kong and recommend to the Financial Secretary through EFAC measures to enhance the robustness and effectiveness of Hong Kong's currency board arrangements.

The HKMA pursues a policy of transparency to ensure that the financial industry and the wider public are fully informed of the currency board operations.

The Government is fully committed to the maintenance of the linked exchange rate system, which is a cornerstone of Hong Kong's monetary and financial stability, and to the strict discipline of the currency board arrangement under that system.

Monetary Situation

Having withstood the global financial crisis in 2008, the effective functioning of the Linked Exchange Rate system continued to keep the Hong Kong dollar stable in 2009. Despite large swings in the US dollar, activities in the local foreign exchange market were generally orderly. The Hong Kong dollar market exchange rate stayed within a narrow range between 7.7500 and 7.7594 for most of the time.

After stabilising towards the end of 2008, the Hong Kong interbank money market largely returned to normal in 2009. The various liquidity measures introduced in 2008 were effective. Liquidity concerns eased and confidence in the local banking system strengthened. Term interbank interest rates declined to very low levels during the year, reflecting the larger Aggregate Balance and the downward movements in the corresponding US dollar interest rates. The overnight interbank interest rates also stayed near zero, with occasional increases due to IPO-related funding demand.

The HKMA exited from the five temporary liquidity measures and other related policy actions in March 2009 smoothly and Hong Kong's money market remained calm. The HKMA also prepared the ground for exiting from the contingent capital facility for banks and the temporary full deposit guarantee, although there had been no need to resort to these measures. In July 2009, the HKMA, Bank Negara Malaysia and the Monetary Authority of Singapore established a tripartite working group to facilitate the scheduled exit from the full deposit guarantees by the end of 2010 in their respective jurisdictions. Meanwhile, the Government is preparing legislative amendments to effect the enhancements to the Deposit Protection Scheme so that the public may enjoy better deposit protection under an enhanced Deposit Protection Scheme upon the expiry of the full deposit guarantee.

Exchange Fund

According to the Exchange Fund Ordinance, the Exchange Fund's primary statutory role is to affect the exchange value of the Hong Kong dollar. It can also be used to maintain the stability and integrity of the monetary and financial systems, with a view to maintaining Hong Kong as an international financial centre.

The HKMA is responsible to the Financial Secretary for the use and the investment management of the Exchange Fund. To meet the objectives of preserving capital, providing liquidity to maintain financial and currency stability and generating an adequate long-term return, the Exchange Fund is managed as distinct portfolios. The Backing Portfolio holds highly liquid US-dollar-denominated debt securities to fully back the monetary base. The Investment Portfolio aims to preserve the fund's long-term purchasing power. The asset allocation strategy of the Exchange Fund is guided by the investment benchmark approved by the Financial Secretary on the advice of the EFAC. The details of the management of the fund and the investment style adopted are set out and explained in the HKMA's annual report. A Strategic Portfolio was set up in 2007 to hold all the shares of Hong Kong Exchanges and Clearing Limited acquired for strategic purposes by the Financial Secretary using the Exchange Fund.

On December 31, 2009, the Exchange Fund's total assets stood at $2,151.7 billion. The accumulated surplus of the Exchange Fund amounted to $553.3 billion. Foreign currency asset figures have been published monthly since January 1997 to demonstrate the Government's continued commitment to greater openness and transparency. In addition, an abridged balance sheet of the Exchange Fund and a set of Currency Board accounts are published monthly.

Another function related to the Exchange Fund is currency issuance. Bank notes in denominations of $20, $50, $100, $500 and $1,000 are issued by the three note issuing banks: Standard Chartered Bank (Hong Kong) Limited, the Hongkong and Shanghai Banking Corporation Limited and Bank of China (Hong Kong) Limited. The note-issuing banks may issue currency notes only by surrendering non-interest bearing US dollar backing at a fixed exchange rate of $7.80.

Through the HKMA, the Government issues $10 currency notes and coins of $10, $5, $2, $1, 50 cents, 20 cents and 10 cents denominations. The Hong Kong $10 polymer note was put into circulation in July 2007. The HKMA, which has been examining alternative technologies for the production of currency notes, issued the note to assess the performance and acceptability of polymer notes in Hong Kong. The value of all notes and coins in circulation at year-end was $208.4 billion.

Websites

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