

# Financial and Monetary Affairs

*As Asia's premier international financial centre, Hong Kong ranked third of 80 financial centres in the latest Global Financial Centres Index and its stock market ranked first globally in terms of equity funds raised through initial public offerings in 2015. Hong Kong is the world's largest offshore Renminbi (RMB) market, offering a diversified range of products. The financial sector has a 246,000-strong workforce, accounting for 6.5 per cent of the city's total workforce and 16.6 per cent of the local economy.*

## **Hong Kong as an International Financial Centre**

### **Overview**

Hong Kong, located at the heart of Asia, plays a vital part in the 24-hour continuous trading system worldwide together with New York and London. It also holds a unique position in the increasingly integrated global financial system, in particular through its extensive geographical, cultural and linguistic links with the dynamic Mainland economy and financial system.

The robust financial services industry in Hong Kong is built on its excellent communications with the rest of the world; the rule of law; a level playing field for conducting business; a sound regulatory regime; an absence of restrictions on capital flows into and out of Hong Kong; an emphasis on investor protection; and a well-educated workforce and ease of entry for professionals from outside the city. Hong Kong's financial markets offer a high level of liquidity and are governed by effective and transparent regulations that are in line with international standards.

It is therefore not surprising that Hong Kong's competitiveness as an international financial centre is well recognised. The Global Financial Centres Index published by Z/Yen Group in September ranked Hong Kong as the third global centre, behind only New York and London. An International Monetary Fund (IMF) Mission, following the 2015 Article IV Consultation, affirmed that Hong Kong's robust financial system and prudent fiscal management would help deal with near-term challenges while laying the foundations for steady growth and healthy job creation in the medium term.

### **Vibrant Securities and Derivatives Market**

The city's stock market capitalisation, at about \$24.7 trillion at the end of 2015, ranked eighth in the world and fourth in Asia. At the end of the year, 1,866 public companies were listed on the

Stock Exchange of Hong Kong Limited (SEHK), representing a wide range of industries from finance and property to resources and telecommunications. In 2015, the SEHK ranked first worldwide in terms of initial public offering (IPO) equity funds raised, at \$263 billion. In addition to new share issues, another \$853 billion was raised on the secondary market, ranked third globally. Daily turnover reached a record high of \$105.6 billion, a 52 per cent increase compared to 2014. Moreover, the turnover of securitised derivatives of the Hong Kong Exchanges and Clearing Limited (HKEx) has ranked first in the world since 2007.

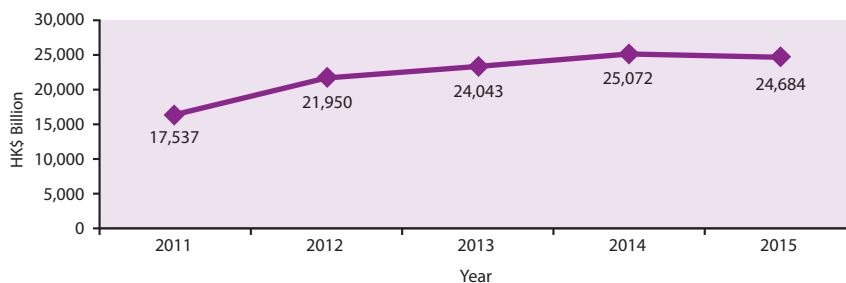
At the end of 2015, 951 Mainland enterprises were listed on the SEHK, raising \$5.1 trillion from the Hong Kong market since 1993. Hong Kong is also a listing destination for international companies. Funds raised by international and Mainland companies represented 94 per cent of IPO equity funds raised in 2015.

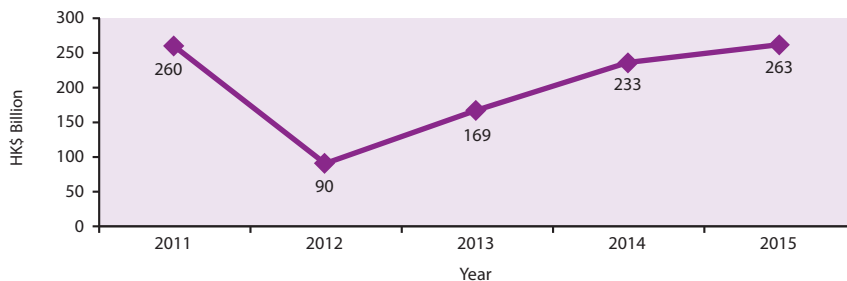
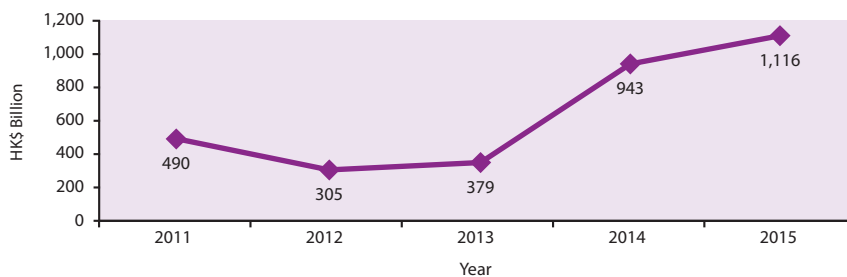
The Hong Kong Futures Exchange Limited (HKFE) operates a futures market. Total turnover of derivatives contracts in 2015 was 190 million, the highest ever and an increase of 33.3 per cent from 2014, largely driven by strong trading in stock options and index futures and options. Open interest at the year end was 7.3 million contracts.

As an international and open market, Hong Kong attracts many intermediaries from other markets to set up companies locally and most international brokerages have branches in the city. At the end of 2015, 27.2 per cent of the 515 SEHK trading participants were from the Mainland or overseas markets, and 50.3 per cent of the 179 HKFE trading participants were from those markets.

The HKEx operates four clearing houses, namely, Hong Kong Securities Clearing Company Limited, HKFE Clearing Corporation Limited (HKCC), SEHK Options Clearing House Limited and OTC Clearing Hong Kong Limited, providing integrated clearing, settlement, depository and nominee services for its participants and members.

**Chart 1** Market Capitalisation of Stock Market

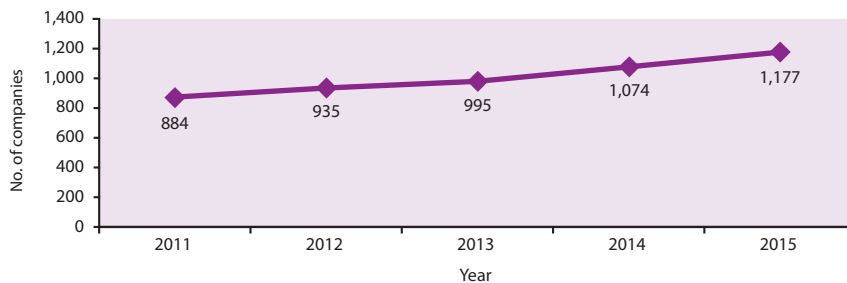


**Chart 2** Equity Funds Raised Through IPOs**Chart 3** Total Equity Funds Raised**Asset Management Hub**

Hong Kong is well placed to become Asia's premier asset management centre amid a huge demand for wealth and asset management services on the Mainland and elsewhere in Asia. The asset management business is highly international, with about 71 per cent of the assets under management coming from investors outside Hong Kong.

The city has a strong asset management foundation and world-class financial infrastructure. At the end of 2015, 1,177 companies were licensed or registered to carry out asset management business locally, marking a rise of 9.6 per cent from the end of 2014.

The government, together with other agencies, works to provide a conducive operational, regulatory and tax environment to grow a full spectrum of asset management activities.

**Chart 4** Number of Asset Management Companies

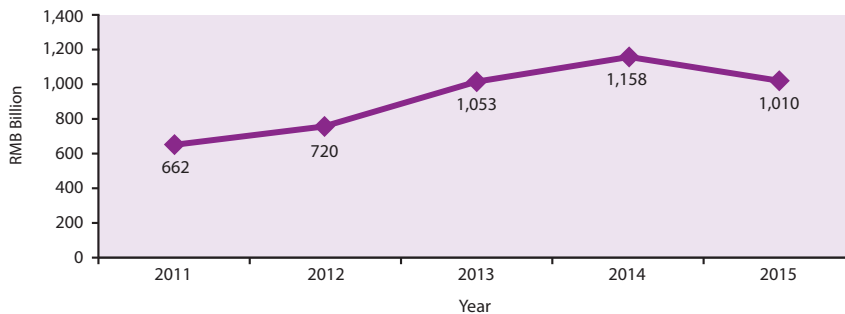
### Largest Offshore RMB Centre

Amid the further internationalisation of RMB, the currency has been increasingly used in cross-border transactions, investment, financing and asset management. Hong Kong continues to be the world's leading and largest offshore RMB business hub, with the world's largest pool of offshore RMB funds and the widest variety of RMB-denominated investment products.

At the end of 2015, total RMB deposits, including customer deposits and outstanding certificates of deposit, stood at RMB1,010.4 billion. Apart from the sizeable liquidity pool, Hong Kong offers a wide range of products, including listed and unlisted investment funds, insurance products, currency futures, real estate investment trusts, shares and derivatives products.

Following the launch of the Shanghai-Hong Kong Stock Connect in November 2014, the Mainland-Hong Kong Mutual Recognition of Funds Arrangement was implemented in July 2015, further deepening mutual access between the Mainland and Hong Kong capital markets, enriching the range of RMB-denominated investment products in Hong Kong and promoting the internationalisation of RMB.

**Chart 5 RMB Deposits and RMB Certificates of Deposit**



### International Banking and Payment Centre

Hong Kong was the world's seventh and Asia's second largest banking centre in terms of external positions<sup>1</sup> in the Bank for International Settlements Quarterly Review for the end of 2015.

International financial institutions maintain a strong presence in Hong Kong. Of the world's top 100 banks, 74 operate in the city. At the year end, 150 of the 157 licensed banks in Hong Kong were beneficially owned by parties outside Hong Kong.

The interbank money market is well established. Hong Kong dollar (HKD) wholesale deposits are traded actively among local authorised institutions (AIs), and between local and overseas AIs, recording an average daily turnover of \$276.5 billion in 2015.

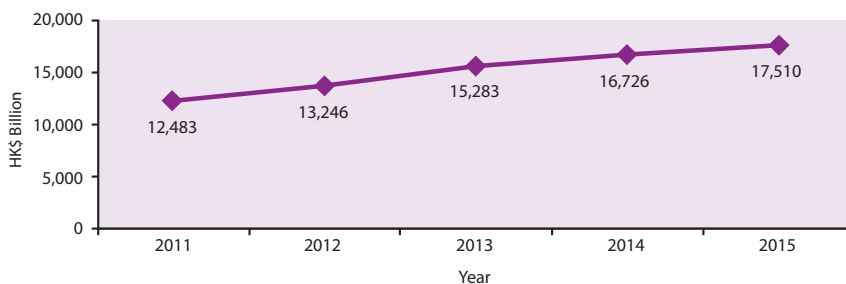
<sup>1</sup> Sum of liabilities to banks and non-bank customers outside Hong Kong and claims on banks and non-bank customers outside Hong Kong, such as equities, securities and capital instruments.

Hong Kong has a robust real-time gross settlement (RTGS) interbank payment system. All banks in the city maintain settlement accounts with the Hong Kong Monetary Authority (HKMA) through the HKD RTGS system. The banks may obtain intra-day and overnight liquidity through repurchase agreements with the HKMA using Exchange Fund Bills and Notes (EFBNs) and government bonds as collateral.

US dollar (USD), euro and RMB RTGS systems enable transactions in these currencies to be settled in real time. All four RTGS systems are linked to enable foreign exchange transactions to be settled on a payment-versus-payment basis.

The HKMA's Central Moneymarkets Unit (CMU) provides clearing, settlement and custodian services for EFBNs, government bonds and other HKD or foreign currency public/private debt securities. It is linked to a number of international and regional central securities depositories to enable overseas investors to hold and settle securities lodged with the CMU and local investors to hold and settle securities lodged with overseas systems. Through its seamless interface with the RTGS systems, the CMU system is able to settle securities transactions on a delivery-versus-payment basis. Besides debt securities, the CMU provides a standardised and automated platform for the investment fund industry to streamline the handling of investment fund order instructions.

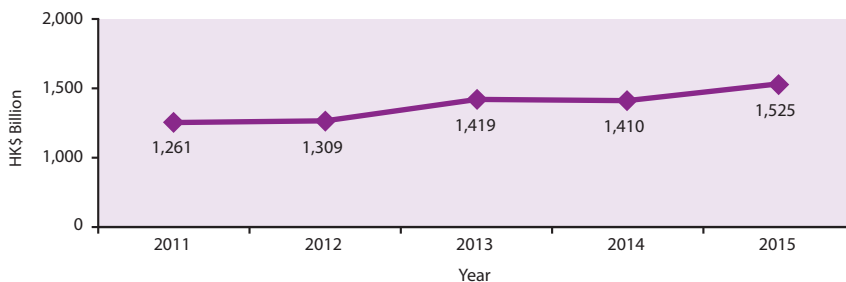
**Chart 6 External Positions of AIs**



### **Bond Market Development**

Outstanding HKD debt securities, including EFBNs, totalled \$1,525 billion at the end of 2015.

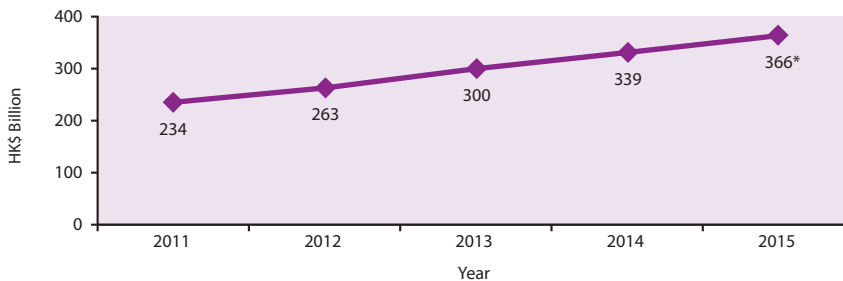
**Chart 7 Total Outstanding HKD Debt Securities**



### Open Insurance Market

Hong Kong continues to be one of the most open insurance centres in the world. Of the 157 authorised insurers at the end of 2015, 71 were from the Mainland or one of 21 overseas jurisdictions. In addition, 14 of the world's top 20 insurers were authorised to conduct insurance business in Hong Kong either directly or through a group company. The city had 19 professional re-insurers, including most of the world's top re-insurers. Gross premium income was \$365.77\* billion, representing an increase of 7.8 per cent over 2014.

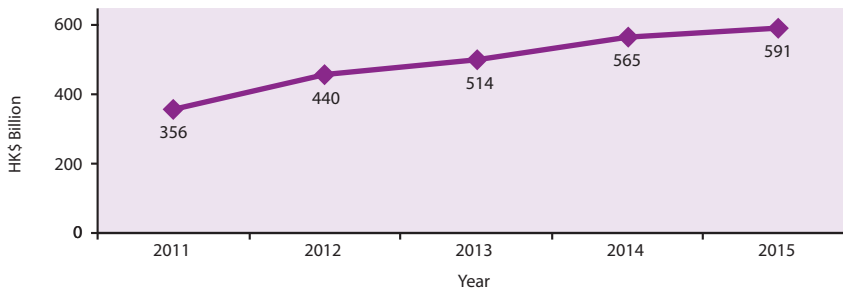
**Chart 8 Annual Gross Premiums of Insurance Market**



### Mandatory Provident Fund

Mandatory Provident Fund (MPF) schemes had a net asset value (NAV) of \$591 billion at the end of 2015 and an annualised rate of return of 3 per cent between December 2000, when the MPF System was launched, and December 2015.

**Chart 9 Total NAV of MPF Schemes**



### Product Offerings in Commodity Trading

Hong Kong operates one of the most active physical gold markets in the world and is one of Asia's largest over-the-counter gold trading centres. Spot gold can be traded through two closely related yet independent markets: the Chinese Gold and Silver Exchange Society and the

\* Provisional statistics.

Loco London gold market. The society provides trading of both tael and kilo bars<sup>2</sup>. Prices track closely those in the major gold markets in London, Zurich and New York.

In addition to operating Hong Kong's securities and derivatives markets, the HKEx owns the London Metal Exchange (LME), the world centre for industrial metals trading and price-risk management. About 80 per cent of global non-ferrous business is conducted on the LME and its prices are used as the global benchmarks. The average daily volume for 2015 was 670,189 lots. The LME launched an in-house clearing house in London in 2014, LME Clear, to support the exchange's commodity business.

## Major Initiatives

Continuous efforts were made in 2015 to enhance Hong Kong's competitiveness as an international financial centre through striking an adequate balance between regulations and promoting market development. The government continues to press ahead with various initiatives to consolidate the city's leading role as the Asia-Pacific region's asset management centre, advance financial co-operation with the Mainland, further develop offshore RMB business and enhance the functions of its funding platform. The government also encourages the use of technology to enhance operational efficiency and foster innovative modes of services in the financial services industry. At the same time, the government works closely with regulators and the industry to align with the international regulatory reform agenda to promote stability of the financial system, improve market quality and strengthen investor protection.

## Enhancing Hong Kong's Competitiveness as International Financial Centre

The city will capitalise on opportunities arising from the implementation of the National 13th Five-year Plan and the Belt and Road Initiative to consolidate and enhance its position as a major platform of capital raising and financing for Mainland and overseas enterprises as well as a global hub for offshore RMB business.

The financial services industry also provides a catalyst for the growth of related sectors, such as professional and commercial services. High-quality financial services underpin Hong Kong's position as an international business hub, helping local enterprises to seize business opportunities and attracting Mainland and overseas companies to use the city as a platform for raising funds and developing regional business.

## Fund-raising Centre

In 2015, the SEHK ranked first worldwide in terms of the IPO equity funds raised, at \$263 billion. It attracted 138 new listings, including 14 transfers of listing from the Growth Enterprise Market to the Main Board. Apart from Mainland and Hong Kong companies, five overseas companies, from Japan, Singapore, South Korea and the United States, also listed on the SEHK. Newly listed companies are attracted by the market's liquidity and access to investors across Asia. The SEHK is working to accept more overseas jurisdictions as places of incorporation.

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<sup>2</sup> Tael bars are of 99 per cent fineness and weighted in taels. One tael equals about 1.20337 troy ounces. Kilo bars are of 999.9 parts per thousand fineness and weighted in kilograms.

### ***Developing an Uncertificated Securities Regime***

The Securities and Futures and Companies Legislation (Uncertificated Securities Market Amendment) Ordinance 2015 was enacted in March to enable the introduction of an uncertificated securities market regime in Hong Kong, subject to the formulation of detailed operational rules. This will enhance the securities market's overall efficiency and competitiveness, strengthen corporate governance, improve investor protection and facilitate market development.

### ***Asset Management and Private Wealth Management***

The combined fund management business was valued at \$17,682 billion at the end of 2014. About 71 per cent came from non-local investors, indicating that overseas investors see Hong Kong as a preferred investment platform<sup>3</sup>. At the end of 2015, there were 2,110 unit trusts and mutual funds authorised by the Securities and Futures Commission (SFC)<sup>4</sup>. Among those funds, 636 were domiciled in Hong Kong, up 11 per cent from a year earlier.

To enhance the operational, regulatory and tax environment for fund managers, the government has been taking forward a number of measures to further develop the business. On 17 July, profits tax exemption for offshore funds was extended to private equity funds to attract more private equity funds to expand their business in Hong Kong. Offshore private equity funds are exempt from profits tax in respect of profits derived from specified transactions. This applies to transactions carried out from 1 April.

The government is proposing to introduce an open-ended fund company structure as an alternative fund vehicle. This aims to allow funds to be set up in an open-ended structure like a company, but with the flexibility, not enjoyed by conventional companies, to create and cancel shares for investors to trade the funds. This additional choice would help attract more funds to use Hong Kong as their base. The relevant legislative proposals had been finalised for introduction into the Legislative Council in January 2016.

### ***Exchange Traded Funds (ETFs)***

The government has waived the stamp duty for the transfer of all ETFs from 13 February, when the Stamp Duty (Amendment) Ordinance 2015 took effect. This will promote the development, management and trading of ETFs in Hong Kong. Thirteen new ETFs were authorised in 2015, bringing the number of SEHK-listed ETFs to 133 at the end of the year.

### ***Enhanced Fund Authorisation Process***

In October, the SFC announced starting an enhanced fund authorisation process on 9 November to shorten the overall processing time for new fund applications. Introduced under a six-month pilot arrangement, the enhanced process adopts a 'two-stream' approach: standard applications are fast-tracked with the aim that authorisation, if granted, will be given on average

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<sup>3</sup> Figures are quoted from the Fund Management Activities Survey for 2014, a survey conducted by the SFC annually to collect information on the general state of affairs in the local fund management industry.

<sup>4</sup> This includes 119 MPF pooled investment funds offered both as retail unit trusts and for mandatory provident fund purposes.



between one and two months from take-up, while authorisation for non-standard applications, if granted, will be given on average within two to three months from take-up. After the pilot period, the SFC will make refinements where appropriate before formally adopting the policy.

### ***Corporate Treasury Centres***

Hong Kong is Asia's premier location for multinational corporations to manage their global or regional treasury functions. To attract more companies to establish corporate treasury centres (CTCs) in Hong Kong, the government introduced the Inland Revenue (Amendment) (No. 4) Bill 2015 into LegCo in December to allow, under specified conditions, interest deductions under profits tax for CTC, and to reduce the profits tax rate for qualifying CTCs by 50 per cent, lowering it to 8.25 per cent.

### ***Bond Market and Islamic Finance***

The Government Bond Programme (GBP) promotes the sustainable development of the bond market. It has a borrowing ceiling of \$200 billion.

Bonds totalling \$20.4 billion were issued to institutional investors under the GBP in 2015. In August, the government issued a \$10 billion inflation-linked retail bond (iBond), with a tenor of three years, for the fifth time under the programme to Hong Kong residents to further develop the retail bond market.

To promote the development of the Islamic bond (sukuk) market, the government issued US\$1 billion, five-year government sukuk in June under the GBP. The offer attracted orders of US\$2 billion from a diverse group of international investors. The sukuk was in Wakalah structure, making Hong Kong the first AAA-rated government sukuk issuer to adopt this structure and demonstrating the flexibility of Hong Kong's issuance platform.

### ***Financial Technologies (Fintech)***

Fintech can enhance the operational efficiency of financial institutions and foster new modes of development for the financial services industry. Hong Kong, as an international financial centre with a highly developed information and communication technology sector, is an ideal hub for developing Fintech. To spearhead the development of the Fintech sector, the government set up a Steering Group on Fintech in April to develop recommendations on how to promote the city as a Fintech hub in collaboration with the regulatory authorities, tapping the minds of industry professionals, the academia, and research and development institutions.

### ***Improvement of Corporate Insolvency Law***

The Companies (Winding Up and Miscellaneous Provisions) (Amendment) Bill 2015 was introduced into LegCo in October. The bill aims to improve and modernise Hong Kong's corporate winding-up regime with a view to increasing protection of creditors, streamlining the winding-up process and further enhancing the integrity of the process.

### ***Financial Services Development Council***

The Financial Services Development Council, established by the government in 2013, published seven reports in 2015, providing proposals on subjects including Chinese enterprises going

global, asset management, booking of transactions by financial institutions and human capital. The government seeks to implement such recommendations where appropriate to boost the financial services industry and will strengthen support for the council's work as a high-level, cross-sectoral government advisory body in collecting industry views to formulate strategic proposals for the development of the industry.

### **Improving Market Quality and Financial Consumer Education and Protection**

Adequate investor protection is essential to promote confidence in the financial system. International financial centres have pursued a series of regulatory reform initiatives to enhance the resilience and stability of the global financial system. The government will continue to drive, facilitate and co-ordinate initiatives to ensure the overarching framework would enhance protection for investors and promote market development in the face of both global needs and local circumstances.

#### ***Basel III Implementation***

Hong Kong follows the international timeline of the Basel Committee on Banking Supervision (BCBS) in implementing the Basel III reform package. Amendments to the Banking (Capital) Rules, and the Banking (Liquidity) Rules, came into effect on 1 January to introduce capital buffers and a new liquidity framework.

#### ***Regulation of Over-the-counter Derivatives***

The Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules were gazetted in May and implemented in July, beginning the first phase of mandatory reporting and related record-keeping obligations for over-the-counter (OTC) derivative transactions. In September, the SFC and the HKMA began a joint consultation on introducing the first phase of mandatory clearing and the second phase of mandatory reporting.

The SFC also published a consultation paper on proposed changes to update the Guidelines for the Regulation of Automated Trading Services, which reflect regulatory and market developments and provide more specific requirements for central counterparties that wish to provide clearing services for OTC derivative transactions.

In July, the SFC launched a consultation on proposed changes to the Securities and Futures (Financial Resources) Rules relating to capital and other prudential requirements for licensed corporations engaged in OTC derivatives activity. The proposals aim to ensure licensed corporations maintain their capital and liquidity at levels which are commensurate with the risks they undertake as well as to encourage them to adopt more advanced risk management standards.

#### ***Developing an Effective Resolution Regime for Financial Institutions***

Following substantial publicly funded bailouts of financial institutions in the global financial crisis, the Financial Stability Board (FSB) issued its 'Key Attributes of Effective Resolution Regimes for Financial Institutions' in 2011 and reissued them in October 2014. The key attributes set standards in respect of those powers that FSB member jurisdictions are expected to have in

place so problems in systemically important financial institutions may be resolved in a way that protects financial stability, including the continued performance of critical financial services, without exposing taxpayers to loss.

As an FSB member jurisdiction, Hong Kong is committed to implementing these standards and needs legislative reform to achieve this. Following the first stage of public consultation in 2014, the government, in conjunction with the financial regulators, launched a second consultation in January 2015 to seek views on specific aspects of the proposed regime, including further details on the resolution options and powers proposed in the first consultation paper, and the governance arrangements and safeguards. The government released the consultation outcome in October and introduced the Financial Institutions (Resolution) Bill into LegCo in December.

### ***Anti-Money Laundering and Counter Financing of Terrorism***

Anti-money laundering and counter financing of terrorism (AML/CFT) was a key focus area for financial regulators that strengthened specialist resources and supervision of financial institutions' AML/CFT programmes. The government and financial regulators play an active role in relevant international standard-setting bodies, such as the Financial Action Task Force, to ensure Hong Kong's AML/CFT regime is in line with those standards and practices.

### ***Enhanced Regulation of SFC-authorized Investment Products***

In January, the SFC amended the Code on Unit Trusts and Mutual Funds to give authorised funds greater flexibility in determining the means for making public their offer and redemption prices, NAVs and notices of dealing suspension. The code was amended also to increase the frequency at which prices and NAVs are disseminated.

### ***E-cheques and Regulation of Stored-value Facilities and Retail Payment Systems***

With support from the government, an e-Cheque service was launched in December, providing a convenient, safe and environmentally friendly means for bank customers to issue and deposit cheques online.

The Payment Systems and Stored Value Facilities Ordinance took effect on 13 November. Under the ordinance, the HKMA is empowered to implement a licensing system for stored-value facilities, and designate retail payment systems to ensure their safe and robust operations under prudential regulation.

### ***Independent Insurance Authority***

The policy objectives of setting up an independent Insurance Authority (IIA) are to modernise the regulatory infrastructure to facilitate the insurance industry's stable development, provide better protection for policyholders, and align with international practice that financial regulators should be financially and operationally independent of the government. The Insurance Companies (Amendment) Ordinance 2015 (IC(A)O) was enacted on 10 July, providing for a legal framework to establish an IIA and a statutory licensing regime for insurance intermediaries to replace the existing self-regulatory system.

The IC(A)O will take effect in three stages to allow for a smooth transition from the existing regime to the IIA-administered regime. The Chairman and members of the IIA were appointed by the Chief Executive and took office in December. Pursuant to the ordinance, the IIA has been renamed the Provisional Insurance Authority (PIA). The PIA is vested with administrative powers to undertake essential preparatory work for the IIA to take over the functions of the Office of the Commissioner of Insurance and the three existing Self-regulatory Organisations during the next stages.

### ***Risk-based Capital Framework for Insurance Industry***

In September, the Insurance Authority (IA) released the conclusions of a consultation on a proposed Risk-based Capital (RBC) framework for the local insurance industry. The framework seeks to align Hong Kong's insurance regime with international standards and make capital requirements more sensitive to the level of risk that insurance companies are bearing. There is general industry support for the move towards an RBC framework. The IA will develop detailed rules and carry out quantitative impact studies before presenting more detailed proposals for further consultation.

### ***Investor Education Centre***

The Investor Education Centre, formed in 2012, seeks to raise financial literacy by providing comprehensive, credible and impartial financial information to better equip the public with the skills and knowledge to make informed financial decisions and to manage their money wisely. Its work is supported by Hong Kong's four financial regulators<sup>5</sup> and the Education Bureau.

During the year, the centre held 158 community events reaching more than 21,500 people, and recorded over 550,000<sup>6</sup> visitors to its website. It also launched the Hong Kong Financial Competency Framework to help establish behavioural standards for the public to emulate and for organisations to utilise when developing their initiatives. A research grant was set up to stimulate financial literacy research and promote robust partnerships between financial education practitioners and academics.

In November, the centre launched Hong Kong's inaugural financial literacy strategy, building on the results of a public consultation, feedback from a series of stakeholder workshops, international best practices and considerable community support. The Hong Kong Strategy for Financial Literacy focuses on raising awareness of the benefits of financial education, extending learning opportunities and enhancing co-ordination and collaboration among stakeholders. As of December 2015, 40 associations have signed up as supporting organisations to promote, together with 11 ambassadors, the benefits of financial education to the public.

### ***Financial Dispute Resolution Centre***

The Financial Dispute Resolution Centre administers in an independent and impartial manner a financial dispute resolution scheme to facilitate the resolution of monetary disputes between individual customers and financial institutions by 'mediation first, arbitration next'. To raise public

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<sup>5</sup> The SFC, the HKMA, the Mandatory Provident Fund Schemes Authority and the OCl.

<sup>6</sup> Aggregation of the monthly number of users who visited the IEC website at least once.

awareness of its services, the centre launched advertising campaigns and other promotional programmes in 2015, including investor education seminars, briefings and interviews, to promote its alternative services to industry professionals and investors.

### ***Auditor Regulatory Reform***

The international trend is for oversight of the regulation of auditors of public interest entities to be independent of the profession itself. In June 2015, the government issued the conclusions of a three-month public consultation conducted in 2014 on proposals to reform the regulatory regime for auditors of public interest entities, that is, listed entities in Hong Kong's context. The government is preparing an amendment bill and will continue to engage stakeholders.

## **Hong Kong as China's Global Financial Centre – Financial Co-operation with the Mainland**

### ***Capital Formation Centre and Global Investment Platform for the Mainland***

Hong Kong is the ideal centre for Mainland enterprises to raise capital. The growing presence of Mainland companies listed on the SEHK in turn has increased the breadth and depth of Hong Kong's securities and futures markets through a greater diversity of constituent stocks in the equity market and a wider range of products. Mainland enterprises also raise capital in Hong Kong through the issuance of bonds, project financing and loan syndication. Moreover, Mainland companies can leverage Hong Kong's position as an international business centre and its world-class investment banking services for mergers and acquisitions to invest in international markets.

### ***Offshore RMB Business***

In 2015, Hong Kong maintained its status as the global offshore RMB business hub and recorded steady growth in a number of areas. RMB trade settlement transactions handled by banks in Hong Kong amounted to RMB6,833.1 billion, up 9.2 per cent from 2014. RMB bank lending expanded by 58.2 per cent to RMB297.4 billion at end-2015 from the beginning of the year. Average daily turnover in the RMB Real Time Gross Settlement system reached RMB947 billion, up 29.2 per cent from 2014. Meanwhile, total RMB deposits, including customer deposits and outstanding certificates of deposit, fell 12.8 per cent to RMB1,010.4 billion at end-2015. RMB bond issuance also moderated to RMB74.6 billion from RMB196.8 billion in 2014.

Hong Kong is also the world's largest offshore RMB investment product market. It offers a wide range of products, including listed and unlisted investment funds, insurance products, currency futures, real estate investment trusts, shares and derivatives products. Qualified institutions continued to show interest in developing Renminbi Qualified Foreign Institutional Investor (RQFII)/Stock Connect products<sup>7</sup> in Hong Kong. The number of fund management companies managing SFC-authorized RQFII/Stock Connect funds increased from 38 at the end of 2014 to 41 at the end of 2015. In 2015, the SFC started allowing overseas fund managers to offer overseas funds in RMB in Hong Kong subject to certain conditions. At the end of 2015, there were 71 SFC-authorized RQFII/Stock Connect unlisted funds with an aggregate NAV of RMB20.8

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<sup>7</sup> The RQFII/Stock Connect unlisted funds and ETFs are Renminbi-denominated funds which primarily invest in Mainland securities markets through either the RQFII quota, Stock Connect or both.

billion, and 24 SFC-authorized RQFII/Stock Connect ETFs adopting dual trading counters trading for the RMB and HKD with an aggregate NAV of RMB32.7 billion. The RQFII scheme continues to promote the development of a broader range of RMB investment offerings in Hong Kong and to strengthen the city's position as the leading offshore RMB centre.

Thirteen Hong Kong insurance companies have received approval to invest in the Mainland's interbank bond market since a pilot scheme for eligible institutions was extended to the city's insurance companies in 2012.

In November 2015, the IMF decided to include the RMB in its Special Drawing Right basket of currencies with effective from 1 October 2016. The decision reaffirmed the status of the RMB as a freely usable currency, and would add impetus to the internationalisation of the RMB and the development of Hong Kong's offshore market.

### ***Shanghai-Hong Kong Stock Connect***

The Shanghai-Hong Kong Stock Connect has been operating smoothly since its launch in November 2014. The programme marks an important step in the opening up of the Mainland's capital markets and the internationalisation of the RMB. It also reinforces Hong Kong's position as a premier international financial centre and the city's role as an offshore RMB business centre.

### ***Mutual Recognition of Funds***

The Mainland-Hong Kong Mutual Recognition of Funds (MRF) arrangement, launched in July, allows qualified Mainland and Hong Kong funds to be offered directly to the public in each other's market after obtaining authorisation or approval under streamlined procedures. The arrangement is a milestone in the opening up of the Mainland's funds market to offshore funds and makes available a wider selection of fund products to investors in both markets. On 18 December, the SFC authorised the first batch of four Mainland funds and the China Securities Regulatory Commission approved the first batch of three Hong Kong funds under the arrangement. As of the end of 2015, the SFC had authorised a total of 13 Mainland funds.

### ***Mainland and Hong Kong Closer Economic Partnership Arrangement***

The Closer Economic Partnership Arrangement (CEPA), which came into force in 2004, gives Hong Kong's financial service providers and professionals greater market access and flexibility in their Mainland operations. 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.

On 27 November 2015, the Central People's Government and the Hong Kong Special Administrative Region Government signed an Agreement on Trade in Services under the CEPA framework, to be implemented on 1 June 2016. The agreement basically achieves liberalisation of trade in services between the Mainland and Hong Kong. The key liberalisation measures cover the areas of accounting, insurance, securities and banking.

## **Banking**

### ***Main Features***

Hong Kong maintains three tiers of deposit-taking institutions: licensed banks (LBs), restricted licence banks (RLBs) and deposit-taking companies (DTCs)<sup>8</sup>. They are known collectively as AIs under the Banking Ordinance and are licensed by the HKMA.

The city has one of the highest concentrations of banking institutions in the world. At the end of 2015, there were 157 LBs, 24 RLBs and 18 DTCs. These 199 AIs maintained a network of more than 1,310 local branches. There were also 63 representative offices of banks incorporated outside Hong Kong.

### ***Hong Kong Monetary Authority***

The HKMA's main functions 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; to promote stability and integrity of the financial system, including the banking system; to help maintain Hong Kong's status as an international financial centre, including the maintenance and development of the city's financial infrastructure, and to manage the Exchange Fund.

The HKMA is an integral part of the government, but operates with a high degree of autonomy, complemented by a high degree of accountability and transparency, and can employ people on terms that differ from those of the civil service to attract personnel of suitable experience and expertise. It is accountable to the Financial Secretary, who is advised by the Exchange Fund Advisory Committee in control of the Exchange Fund.

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 banking and other professions.

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 preserve the stability and effective working of the banking system, while at the same time providing sufficient flexibility for AIs to make commercial decisions.

### ***Recent Developments***

The Hong Kong banking sector remained sound in 2015 despite monetary policy divergence in advanced economies and the build-up of vulnerabilities in emerging market economies. The quality of retail banks' assets remained healthy by historical standards. Liquidity ratios remained well above the regulatory minimum. Locally incorporated AIs continued to be well capitalised.

At the end of 2015, total deposits and loans and advances at AIs increased to \$10,749.8 billion and \$7,534.5 billion respectively, up 6.7 per cent and 3.5 per cent from a year earlier. Total assets also rose 4 per cent to \$19,180.4 billion.

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<sup>8</sup> Only LBs may conduct full banking services, including the provision of current and savings accounts and acceptance of deposits of any size and maturity. RLBs may take deposits of any maturity of \$500,000 or above. DTCs may take deposits of \$100,000 or above with an original maturity of at least three months.

*Statistics on Als*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
Als	201	203	199
Of which:			
LBs	156	159	157
RLBs	21	21	24
DTCs	24	23	18
Local branches of Als	1,384	1,370	1,319
Total deposits (\$ billion)	9,178	10,073.9	10,749.8
Total loans and advances (\$ billion)	6,457.4	7,276	7,534.5
Total assets (\$ billion)	16,943.5	18,435.9	19,180.4

The HKMA continued to keep a vigilant watch over the property mortgage business of Als. It introduced a seventh round of macroprudential measures in February to strengthen Als' resilience against a possible downturn in the property market. These measures included lowering the loan-to-value ratio cap for self-use residential properties of lower value and tightening the debt servicing ratio requirement for second self-use residential properties.

**Securities and Futures**

Hong Kong's securities market is operated by the SEHK and its futures market by the HKFE, both being wholly owned subsidiaries of the HKEx. At the end of 2015, 1,866 companies were listed on the Main Board and the Growth Enterprises Market (GEM) of the SEHK, with a total market capitalisation of about \$24.7 trillion. With improved financial market conditions, the total equity funds raised increased 18.3 per cent in 2015 to \$1,116 billion, while the securities market's total turnover increased 52.1 per cent to \$26.1 trillion, with 53.7 trillion shares traded.

In 2015, 13 new ETFs were authorised, bringing the total number of SEHK-listed ETFs to 133. These funds offer a wide range of investment exposures to world, regional and Mainland indices and commodities for investors. Issuance of ETFs with dual HKD and RMB trading counters also increased significantly, tracking a variety of onshore equity and bond indices as well as commodities. Turnover of ETFs reached \$2.2 trillion.

*Statistics on Securities Market (Main Board and GEM)*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
Number of listed companies (year end)	1,643	1,752	1,866
Total market capitalisation (year end) (\$ billion)	24,043	25,072	24,684
Total equity funds raised (\$ billion)	379	943	1,116
Total securities market turnover (\$ billion)	15,265	17,156	26,091
Total number of shares traded (billion)	34,440	34,287	53,694
Number of derivative warrants (DWs) listed (year end)	4,715	4,938	4,590
Turnover of DWs (\$ billion)	1,783	2,045	4,504
Number of callable bull/bear contracts (CBBCs) listed (year end)	1,620	1,579	1,630
Turnover of CBBCs (\$ billion)	1,269	1,230	1,837
Number of ETFs listed (year end)	116	122	133
Turnover of ETFs (\$ billion)	903	1,168	2,171



In the derivatives market, about 190 million futures and options contracts were traded, 33.3 per cent more than in 2014. Trading of major derivatives products included Hang Seng Index (HSI) Futures with a total turnover of 21.24 million contracts; H-shares Index Futures with a total turnover of 33.38 million contracts; HSI Options with a total turnover of 7.52 million contracts; H-shares Index Options with a total turnover of 15.30 million contracts; and Stock Options with a total turnover of 92.46 million contracts.

*Statistics on Derivatives Market Turnover (million contracts)*

	2013	2014	2015
All options and futures contracts	130	142	190
Of which:			
HSI Futures	20	17	21
H-shares Index Futures	21	22	33
HSI Options	9	8	8
H-shares Index Options	8	9	15
Stock Options	61	75	92

At the end of 2015, there were 31 automated trading services providers, comprising mainly foreign exchanges and regulated entities, authorised by the SFC to provide automated trading services. Such services are provided by means of electronic facilities, instead of a recognised exchange company or a recognised clearing house, to transact or settle transactions in securities or futures contracts.

### **Securities and Futures Commission**

As Hong Kong's statutory securities and futures regulator, the SFC derives its statutory powers from the Securities and Futures Ordinance (SFO). The SFC's work can be divided into five areas: intermediaries, investment products, listings and takeovers, market infrastructure and trading, and enforcement.

**Intermediaries** – The SFC's licensing regime sets standards for industry practitioners seeking to be, and to remain, licensed. It supervises licensed corporations, including stock brokers, investment banks, futures and leveraged forex dealers, fund managers, investment advisers and credit rating agencies, with a particular focus on their business conduct and financial soundness.

**Investment products** – The SFC supports the development of Hong Kong both as an asset management hub and as a premier offshore RMB centre. While facilitating market growth and product innovation, the commission continues to perform its gate-keeping functions in authorising investment products offered to the public and in monitoring their compliance with disclosure and other requirements.

**Listings and takeovers** – The SFC oversees the listing-related functions of the SEHK, and the merger, takeover, privatisation and share buy-back activities of public companies in Hong Kong.

It monitors corporate disclosures under the statutory inside information disclosure regime and vets listing applications alongside the SEHK under the dual filing regime, in addition to enhancing listing rules. It also performs detailed reviews of specific companies and broader thematic reviews of market activities which may signal corporate misconduct.

Market infrastructure and trading – The SFC supervises the HKEx's exchanges and clearing houses, share registrars and automated trading services, including overseas exchanges and clearing houses operating in Hong Kong.

Enforcement – The SFC takes firm and prompt action in combating misconduct and malpractice in the securities and futures markets. It can discipline licensed intermediaries through reprimands, suspension or revocation of licences and imposition of fines. It can also deal with market misconduct cases, such as insider dealing and market manipulation, by criminal prosecution or bringing them directly to the Market Misconduct Tribunal<sup>9</sup>. In addition, the commission can apply to the court for injunctive and remedial orders against wrongdoers in favour of victims. Through criminal, administrative, compensatory and disciplinary actions, it strives to protect the interests of the investing public and send strong deterrent messages to the markets.

The Investor Compensation Company is a wholly owned SFC subsidiary established under the SFO to manage the Investor Compensation Fund. It receives and assesses claims and pays from the fund those claims deemed valid in respect of defaults of authorised intermediaries and financial institutions.

The SFC's powers are subject to both internal controls and external scrutiny, designed to ensure fairness in its decision-making, observance of due process and proper use of its regulatory powers. Specified SFC decisions are subject to review by the Securities and Futures Appeals Tribunal. The commission's procedures, actions and decisions are also subject to other checks and balances, including the Process Review Panel for the SFC, the Ombudsman and the courts.

### **Recent Developments**

At the end of 2015, there were 41,347 licensed entities, including securities brokers, futures dealers, investment advisers and fund managers as well as their representatives, and 119 registered institutions, such as banks, engaging in regulated activities such as dealing in and advising on securities and futures.

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<sup>9</sup> The Market Misconduct Tribunal is an independent body established under the SFO, and is chaired by a judge or a former judge of the High Court who sits with two members.

*Statistics on Licensing for SFC-regulated Activities (year end)*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
Licensed entities	38,985	39,621	41,347
Of which: Licensed corporations	1,956	2,034	2,172
Licensed individual	37,029	37,587	39,175
Registered institutions	121	118	119

In March, the SFC launched a consultation on proposed Principles of Responsible Ownership, which provide guidance on how investors should fulfil their ownership responsibilities in relation to their investment in a Hong Kong-listed company. In May, the SFC published consultation conclusions on proposals to enhance and unify the regulatory regime for alternative liquidity pools<sup>10</sup>. The new regime came into effect on 1 December. In June, the commission published consultation conclusions on proposed amendments to the SFO that involved helping overseas regulators in certain situations. These amendments came into effect on 13 November.

To improve monitoring and enhance market transparency, the SFC began a consultation in November on expanding the scope of short position reporting to cover all securities that can be short sold under SEHK rules. The commission also ended a Further Consultation on the Client Agreement Requirements, which would require a new clause<sup>11</sup> to be incorporated into client agreements under the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

On the enforcement front, the SFC disciplined licensees, including 20 individuals and 12 corporations, with fines totalling \$70.9 million. Separately, 13 individuals and four corporations were successfully prosecuted for criminal offences that included unlicensed activities and market manipulation.

During the year, the SFC obtained a number of compensation orders in favour of investors: it resolved proceedings against a collapsed hedge fund to recover \$191 million in assets for about 340 overseas investors; and received interim orders against an unlicensed investment firm, including freezing its \$23.5 million of assets. The court also ordered a listed company to be wound up, marking the first time the commission obtained an order to wind up a listed company to protect investors. In addition, market Misconduct Tribunal proceedings were commenced against a listed company and its chairman and chief executive officer in the first case related to disclosure obligations.

To reduce the industry's compliance burden and protect the environment, the SFC ceased issuing printed licences to individual licensees from November.

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<sup>10</sup> Also known as alternative trading systems or dark pools.

<sup>11</sup> This enables an investor to claim for damages under the client agreement where the regulated intermediary solicits the sale of or recommends a financial product which is not reasonably suitable.

## Insurance

At the end of 2015, there were 157 authorised insurers, 86 of which were incorporated in Hong Kong while the remaining 71 were incorporated on the Mainland or in overseas jurisdictions.

During the past five years, the Hong Kong insurance industry achieved an average annual growth of 12.3 per cent. In 2015, total gross premiums amounted to \$365.8\* billion, representing an increase of 7.8 per cent over 2014. The total revenue premiums<sup>12</sup> of in-force long-term business rose 8.2 per cent to \$319.8\* billion. Individual life insurance remained the leading business, accounting for \$293.5\* billion, or 91.8\* per cent, of total revenue premiums, while the corresponding number of policies stood at 11.5\* million.

General insurance business rose in money terms to \$46\* billion from \$43.6 billion in 2014, representing a 5.3 per cent increase in gross premiums. The growth was largely led by insurance policies relating to Accident and Health business (comprising Medical business) and General Liability business (comprising Employees' Compensation business). The overall underwriting performance of general insurance business declined from \$3 billion to \$1.7\* billion.

At the end of 2015, there were 90,969 individual insurance intermediaries, comprising 9,397 Chief Executives or Technical Representatives (TRs) of 733 broker firms, 27,723 Responsible Officers or TRs of 2,493 agency firms, and 53,816 individual agents and their 33 TRs.

### Statistics on Insurance Business

	2013	2014	2015
Number of authorised insurers	155	158	157
Of which:			
Incorporated in Hong Kong	85	86	86
Incorporated on the Mainland or overseas	70	72	71
Premium income (\$ billion)	299.5	339.3	365.8*
Total gross premiums			
Of which:			
Long-term in-force business (Office/Revenue premiums)	257.7 <sup>^</sup>	295.7 <sup>^</sup>	319.8* <sup>#</sup>
General insurance (Gross premiums)	41.8	43.6	46.0*

<sup>^</sup> Office premiums

<sup>#</sup> Revenue premiums

\* Provisional statistics

<sup>12</sup> The premiums actually received during the financial year.

### **Insurance Authority**

The Commissioner of Insurance is appointed by the Chief Executive as the IA under the Insurance Companies Ordinance with the principal function of regulating and supervising the insurance industry to promote its general stability and protect policyholders<sup>13</sup>. The Insurance Advisory Committee advises the Chief Executive on matters relating to the administration of the Insurance Companies Ordinance and the carrying on of insurance business in the city.

As a member of the International Association of Insurance Supervisors (IAIS), Hong Kong is also required to observe international principles and standards in its insurance supervisory regime. The IA works closely with regulators in other jurisdictions in regulating major insurance groups and continues to take part in supervisory colleges organised by the home regulators of such groups.

### **Recent Developments**

To enhance the standards of conduct and promote sound and prudent business practices among insurers, the IA issued a guidance note on underwriting investment-linked assurance schemes (ILAS) business which came into operation on 1 January. The note had made reference to a 'fair treatment of customers' principle announced by the IAIS, and sets out comprehensive requirements, including the design of ILAS products, sales processes, remuneration of intermediaries and post-sale control requirements.

To extend the principle of fair treatment of customers to all life insurance policies, the IA issued another guidance note on 30 July about underwriting life insurance policies other than ILAS. The note will take effect from 1 April 2016 for new insurance products and 1 January 2017 for new and existing insurance policies of current products.

### **Mandatory Provident Fund Schemes and Occupational Retirement Schemes**

The MPF System is a system of privately managed, employment-related mandatory provident fund schemes for the Hong Kong workforce to save for retirement. Unless exempted, employees and self-employed persons aged 18 to 64 are required to join an MPF scheme.

An employer is required to contribute 5 per cent of an employee's relevant income (RI) as mandatory contribution for the employee, subject to a maximum RI level for MPF contribution purposes. Employees are required to make the same contributions for themselves unless their income is below the minimum RI level. Self-employed persons (SEPs) must also contribute 5 per cent of their RI, subject to the minimum and maximum RI levels.

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<sup>13</sup> The Insurance Companies Ordinance 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 ordinance against an insurer to safeguard the interests of policyholders.

The ordinance also sets out a 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.

With effect from 1 November 2012, the IA assumed the statutory role of ensuring compliance by MPF intermediaries from the insurance sector with the conduct requirements stipulated in the Mandatory Provident Fund Schemes Ordinance.

MPF accrued benefits, that is, accumulated mandatory contributions and investment returns, must be preserved until a scheme member reaches the age of 65 or meets a statutory condition for early withdrawal of benefits.

Occupational retirement schemes operated under the Occupational Retirement Schemes Ordinance (ORSO) are voluntary schemes set up by employers. Before the launch of the MPF System, operators of ORSO schemes had the option to apply for exemption from MPF requirements.

*Statistics on MPF Schemes and MPF-exempted ORSO Registered Schemes (year end)*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
Number of MPF-enrolled participants (Estimated rate)			
Employers	264,400 (99%)	271,500 (99%)	276,000 (100%)
Relevant employees	2,485,300 (100%)	2,506,600 (99%)	2,549,000 (100%)
SEPs	212,400 (62%)	208,000 (66%)	205,000 (68%)
<i>MPF schemes</i>			
Number of registered schemes	41	38	38
Number of approved constituent funds	477	458	459
Aggregate NAV (\$ billion)	514	565	591
<i>MPF-exempted ORSO registered schemes</i>			
Number of schemes	3,601	3,500	3,382
Number of participating employees	351,497	341,894	338,000
Aggregate NAV (\$ billion)	273	278	289

### **Mandatory Provident Fund Schemes Authority**

The Mandatory Provident Fund Schemes Authority (MPFA) was established under the Mandatory Provident Fund Schemes Ordinance to regulate, supervise and monitor the operation of the MPF System. It is also the Registrar of Occupational Retirement Schemes. Its objectives are to ensure compliance with the MPF legislative requirements and protect the interests of scheme members. The MPFA monitors MPF trustees and their service providers, investigates cases of non-compliance, conducts inspections, and takes enforcement actions where necessary. It also arranges programmes to strengthen the public's understanding and publicise new developments of the MPF System, and educate scheme members on MPF investments.

### **Recent Developments**

The Mandatory Provident Fund Schemes (Amendment) Ordinance 2015 was enacted by LegCo in January. It includes legislative amendments to increase flexibility in withdrawing MPF accrued benefits by adding the option of a phased withdrawal of benefits upon retirement or early retirement, to streamline the MPF schemes' operational procedures to provide greater scope for MPF fee reduction, and to enable more effective enforcement to protect scheme members'

interests. Some of the enhancements were implemented in August and the ordinance will take full effect in February 2016.

In November, the government and the MPFA introduced the Mandatory Provident Fund Schemes (Amendment) Bill 2015 to mandate each MPF trustee to provide in each MPF scheme a highly standardised and fee-controlled Default Investment Strategy (DIS) (formerly known as the 'core fund') consistent with the overall objective of retirement savings. The Bill proposes that the total payment of management fees for the DIS must not exceed a daily rate equivalent to an annualised rate of 0.75 per cent of the NAV of the Constituent Funds under the DIS, and adopts an investment strategy which decreases the level of risk according to a scheme member's age. Subject to the scrutiny process, the government and the MPFA plan to implement the DIS in December 2016.

### Companies Registry

The registry administers and enforces most parts of the Companies Ordinance. It registers local and non-Hong-Kong companies and statutory returns, de-registers defunct solvent companies and provides the public with services and facilities for inspecting and obtaining company information kept by the registry. It also processes applications relating to money lenders' licences and maintains a register of money lenders for inspection by the public.

The registry operates as a trading fund department, allowing it to deploy resources more flexibly to meet public demands and expectations.

The registry provides electronic search services through the Cyber Search Centre. More than 99 per cent of company searches are now conducted online. The public may also retrieve company information through the Company Search Mobile Service. Electronic Certificates of Incorporation and Business Registration Certificates can normally be issued together in less than one hour after receipt of the applications through the e-Registry portal. The electronic filing service at the e-Registry portal was enhanced to cover all specified forms on 3 March. Electronic forms can be filed and made available for search within 24 hours to facilitate business.

#### *Companies Registry Statistics*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
New local companies	174,031	167,280	139,209
Local companies on the register	1,162,931	1,272,693	1,288,666
New non-Hong Kong companies	780	811	894
Non-Hong Kong companies on the register	9,258	9,624	10,029

### Bankruptcies, Individual Voluntary Arrangement and Compulsory Winding-up

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

When acting as the trustee-in-bankruptcy or liquidator, the OR or a private-sector insolvency practitioner investigates the affairs of the bankrupt or wound-up company, realises assets and

distributes dividends to creditors. The OR also prosecutes insolvency-related offences under the Bankruptcy Ordinance and the Companies (Winding Up and Miscellaneous Provisions) Ordinance, applies for disqualification orders against unfit company directors of wound-up companies, and monitors the conduct of outside liquidators and trustees, and the liquidation monies.

*Statistics on Bankruptcy Orders, Interim Orders in Individual Voluntary Arrangements (IVAs) and Winding-up Orders*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
Bankruptcy Orders	9,371	9,674	9,750
Interim Orders in IVAs	817	798	588
Winding-up Orders	274	271	305

### **Professional Accountancy**

The Hong Kong Institute of Certified Public Accountants (HKICPA), established under the Professional Accountants Ordinance, performs a wide range of functions, such as registering certified public accountants (CPAs); carrying out practice reviews and regulating the professional conduct and standards of members; setting and maintaining financial reporting, auditing and ethical standards for the profession; and conducting training programmes and qualifying examinations.

*Statistics on CPAs, CPA firms and corporate practices*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
Total number of CPAs	36,094	38,426	39,201
Number of practising CPAs	4,166	4,353	4,428
Number of practising CPA firms	1,246	1,275	1,267
Number of corporate practices	427	467	491

The Hong Kong Financial Reporting Standards, issued by the HKICPA, apply the International Financial Reporting Standards. This is beneficial to Hong Kong because international investors and financial analysts are well acquainted with these standards.

The Financial Reporting Council (FRC), a statutory body established under the Financial Reporting Council Ordinance, is responsible for investigating Hong Kong listed entities' non-compliance with accounting standards as well as their auditors' auditing and reporting irregularities. The FRC reviews financial reports based on a risk-based approach and screens modified auditor's reports of financial statements of entities listed in the city.

*Statistics on FRC's work*

	<b>2013</b>	<b>2014</b>	<b>2015</b>
Number of modified auditors' reports screened	168	171	174
Number of financial reports reviewed under risk-based approach	53	34	42
Number of investigations completed	5	4	9
Number of enquiries completed	2	1	-

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



## Monetary Policy

The city's monetary policy objective is currency stability, defined as a stable external exchange value of the HKD, in terms of its exchange rate in the foreign exchange market against the USD, at around HK\$7.80 to US\$1. This objective is achieved through the Linked Exchange Rate System introduced in 1983. The government is fully committed to maintaining this system, which is a cornerstone of the city's monetary and financial stability, and to the strict discipline of the system's currency board arrangements.

The Linked Exchange Rate System is characterised by currency board arrangements requiring the HKD 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 USD reserves held in the Exchange Fund at the fixed exchange rate of HK\$7.80 to US\$1. In Hong Kong, the monetary base includes the amount of currency notes and coins issued, the Aggregate Balance<sup>14</sup>, and the outstanding amount of EFBNs. Banks have unrestricted access to a Discount Window for overnight liquidity through repurchase agreements using EFBNs as collateral. Under the currency board system, HKD exchange rate stability is maintained through an interest rate adjustment mechanism and the HKMA's commitment to honour the Convertibility Undertaking. In particular, the HKMA undertakes to buy USD from licensed banks at HK\$7.75 to US\$1 (strong-side Convertibility Undertaking) and sell USD at HK\$7.85 to US\$1 (weak-side Convertibility Undertaking). The expansion or contraction in the monetary base arising from these currency board operations leads interest rates for the domestic currency to fall or rise respectively, creating the monetary conditions that automatically counteract the original capital movements and ensuring exchange rate stability.

A Currency Board Sub-Committee under the Exchange Fund Advisory Committee (EFAC) oversees the operation of the currency board system and recommends to the Financial Secretary through the EFAC measures to enhance the robustness and effectiveness of the currency board arrangements.

## Monetary Situation

In 2015, the HKD exchange rate traded within a tight range of 7.750 to 7.767. The strong-side Convertibility Undertaking was triggered repeatedly in April, September and October. Net inflows of \$71.5 billion were recorded in April amid strong equity-related demand for HKD, while combined net inflows of \$155.7 billion were seen in September and October, driven by commercial demand for HKD and conversions of offshore RMB (CNH) into HKD. Separately, with yields of short-dated Exchange Fund Bills (EFBs) trading at very low levels amid abundant liquidity following the inflows, the HKMA issued a total of \$75 billion worth of additional EFBs between August and December to meet banks' strong demand for the papers. The additional issuance brought about a corresponding decline in the Aggregate Balance. Nonetheless, as net inflows exceeded the additional issuance of EFBs during the year, the Aggregate Balance increased from \$239.2 billion at the end of 2014 to \$391.3 billion at the end of 2015.

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<sup>14</sup> Aggregate Balance is 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.

Interbank liquidity remained abundant during the year. The HKD interbank interest rates were little changed compared with last year, with some fluctuations due to equity fund-raising activities and seasonal and quarter-end liquidity demand. Overall, the HKD money market and foreign exchange market continued to operate in an orderly and smooth manner.

## Exchange Fund

The fund's primary statutory role under the Exchange Fund Ordinance is to affect the exchange value of the HKD. 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 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 USD-denominated debt securities to fully back the monetary base. The Investment Portfolio aims to preserve the fund's long-term purchasing power. The Exchange Fund's asset allocation strategy is guided by an investment benchmark approved by the Financial Secretary on the advice of the EFAC<sup>15</sup>. A Strategic Portfolio was set up in 2007 to hold all the shares of the HKEx acquired for strategic purposes by the Financial Secretary using the Exchange Fund. To better manage risks and enhance returns in the medium and long term, the HKMA has been diversifying part of the Exchange Fund's investment in a prudent and incremental manner into a greater variety of asset classes, including private equity and real estate investments housed under the Long-Term Growth Portfolio (LTGP). At the end of 2015, the Exchange Fund's total assets stood at \$3,422.9 billion and its accumulated surplus amounted to \$544.9 billion<sup>16</sup>.

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: Bank of China (Hong Kong) Limited, The Hongkong and Shanghai Banking Corporation Limited and Standard Chartered Bank (Hong Kong) Limited. The note-issuing banks may issue currency notes only by surrendering non-interest-bearing USD backing at a fixed exchange rate of HK\$7.80 to US\$1.

Through the HKMA, the government issues \$10 currency notes and coins in denominations of \$10, \$5, \$2, \$1, 50 cents, 20 cents and 10 cents. The value of all notes and coins in circulation at the end of 2015 was \$371.8 billion.

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<sup>15</sup> The details of the management of the fund and the investment style adopted are set out and explained in the HKMA's annual report.

<sup>16</sup> 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.

**Websites**

Companies Registry: [www.cr.gov.hk](http://www.cr.gov.hk)

Companies Registry e-Registry: [www.eregistry.gov.hk](http://www.eregistry.gov.hk)

Company Search Mobile Service: [www.mobile-cr.gov.hk](http://www.mobile-cr.gov.hk)

Financial Dispute Resolution Centre: [www.fdrc.org.hk](http://www.fdrc.org.hk)

Financial Reporting Council: [www.frc.org.hk](http://www.frc.org.hk)

Financial Services and the Treasury Bureau: [www.fstb.gov.hk](http://www.fstb.gov.hk)

Financial Services Development Council: [www.fsdcc.org.hk](http://www.fsdcc.org.hk)

Hong Kong Exchanges and Clearing Limited: [www.hkex.com.hk](http://www.hkex.com.hk)

Hong Kong Monetary Authority: [www.hkma.gov.hk](http://www.hkma.gov.hk)

Investor Education Centre: [www.hkiec.hk](http://www.hkiec.hk)

Mandatory Provident Fund Schemes Authority: [www.mpfa.org.hk](http://www.mpfa.org.hk)

Office of the Commissioner of Insurance: [www.oci.gov.hk](http://www.oci.gov.hk)

Official Receiver's Office: [www.oro.gov.hk](http://www.oro.gov.hk)

Securities and Futures Commission: [www.sfc.hk](http://www.sfc.hk)