



HONG KONG MONETARY AUTHORITY

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

3 May 2021



DISCUSSION TOPICS

Updates on

- Financial and Economic Environment
- Currency Stability
- Banking Stability
- Financial Infrastructure
- Hong Kong as an International Financial Centre
- Investment Environment and Performance of the Exchange Fund
- Hong Kong Mortgage Corporation



FINANCIAL AND ECONOMIC ENVIRONMENT



GLOBAL ECONOMIC GROWTH FORECASTS

Real GDP Growth

(% year-on-year)

	2020	2021 Forecasts	2022 Forecasts
US	-3.5	6.2	4.1
Euro area	-6.8	4.2	4.3
Japan	-4.9	2.8	2.4
Asia (ex-Japan)	-0.1	7.9	5.2
Mainland China	2.3	8.7	5.5
Hong Kong	-6.1	4.4	3.8

Source: April 2021 Consensus Forecasts



REAL GDP GROWTH IN MAJOR ECONOMIES

% qoq, annualised

50
40
30
20
10
0
-10
-20
-30
-40
-50

2006 2008 2010 2012 2014 2016 2018 2020
(Q4)

% qoq, annualised

50
40
30
20
10
0
-10
-20
-30
-40
-50

Euro area

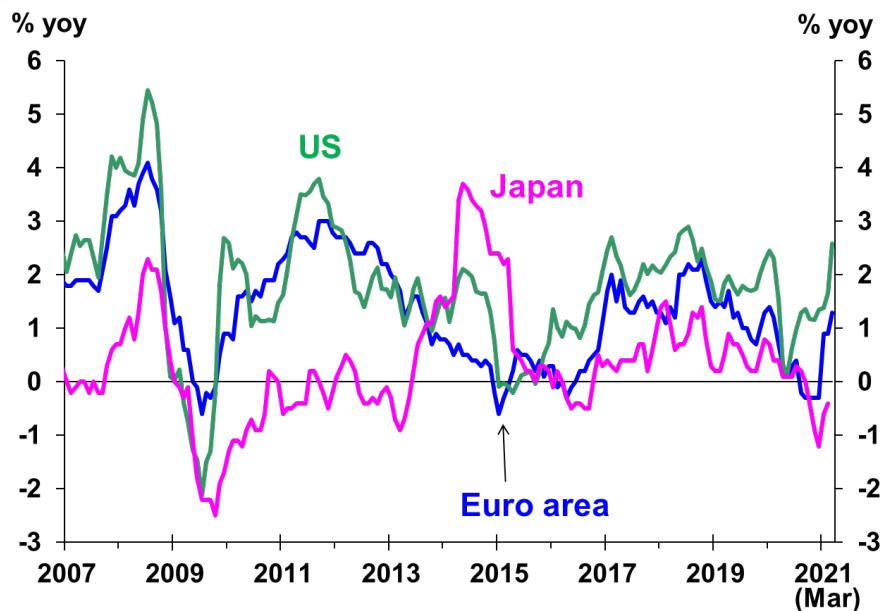
US
Japan

Source: CEIC

5



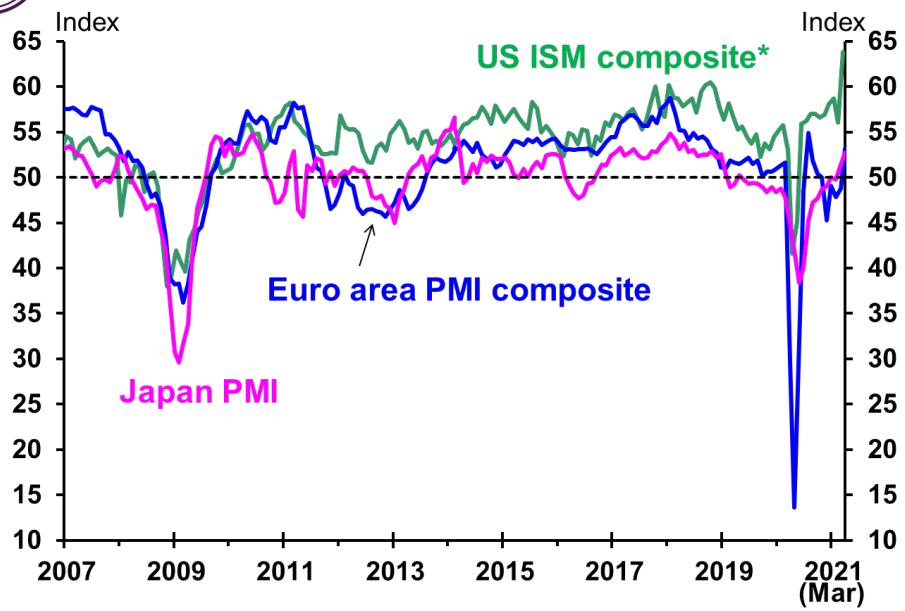
HEADLINE INFLATION IN MAJOR ECONOMIES



Source: CEIC



PURCHASING MANAGERS' INDEX IN MAJOR ECONOMIES

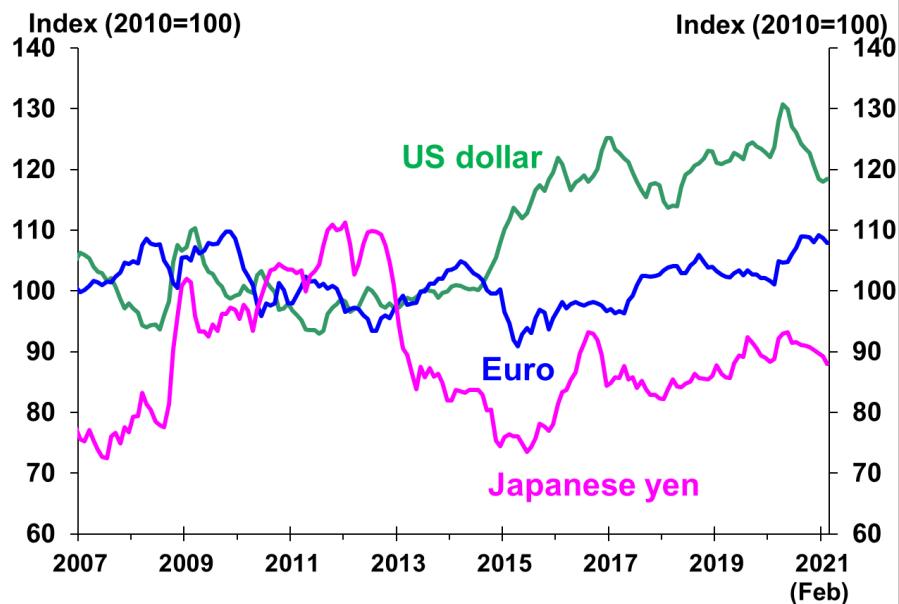


Source: CEIC

7



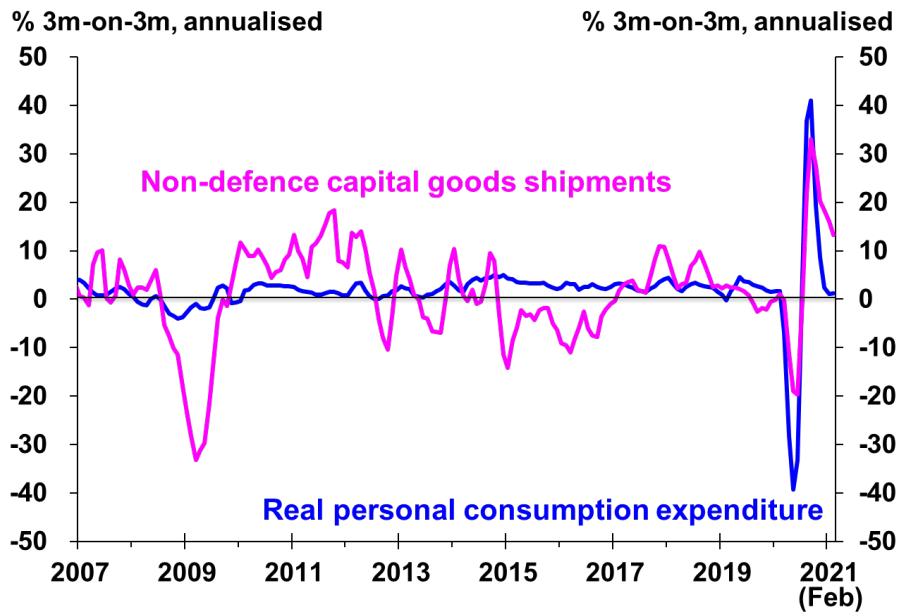
NOMINAL EFFECTIVE EXCHANGE RATE INDEX OF MAJOR CURRENCIES



Source: CEIC



US: CONSUMPTION GROWTH & BUSINESS INVESTMENT ACTIVITY

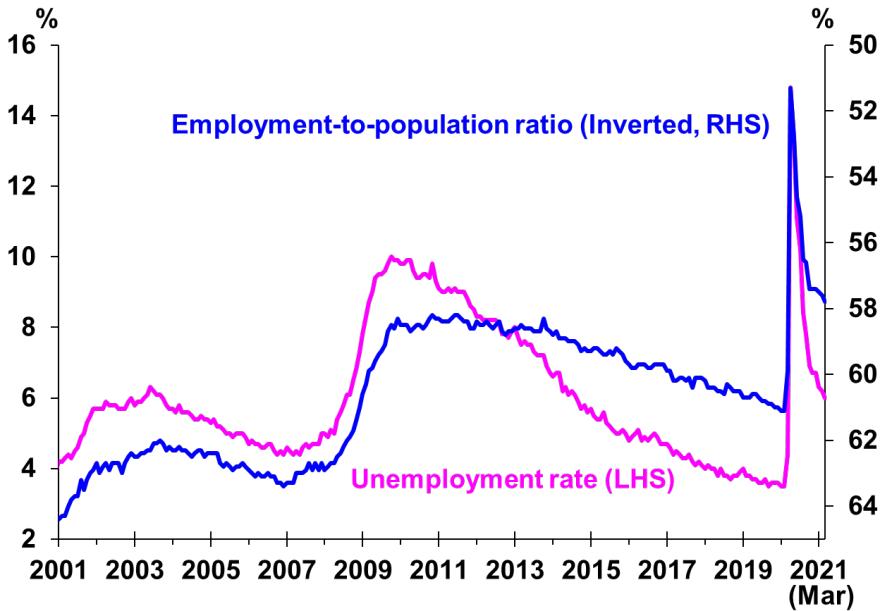


Source: CEIC

9



US: LABOUR MARKET SITUATION



Source: CEIC

10



US: LABOUR FORCE PARTICIPATION

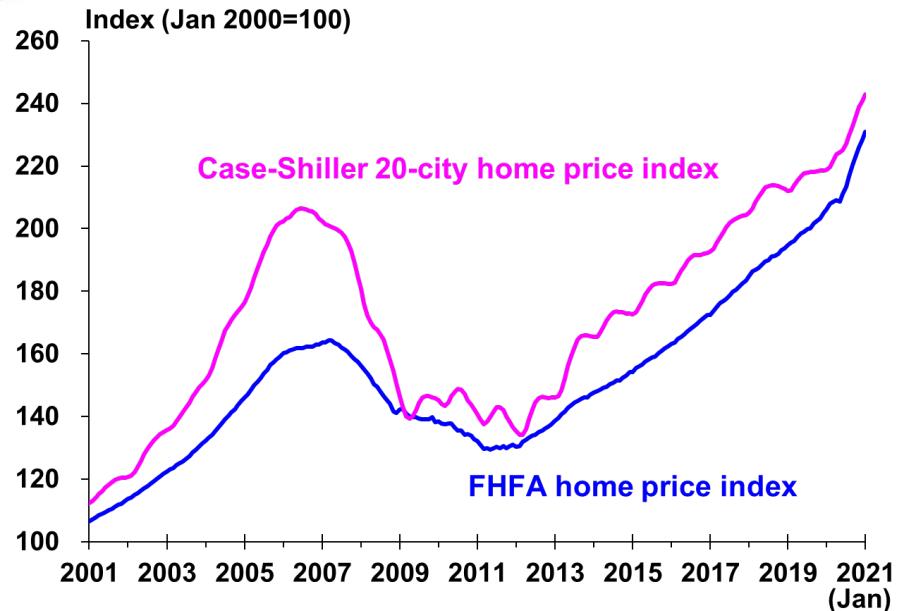


Source: CEIC

11



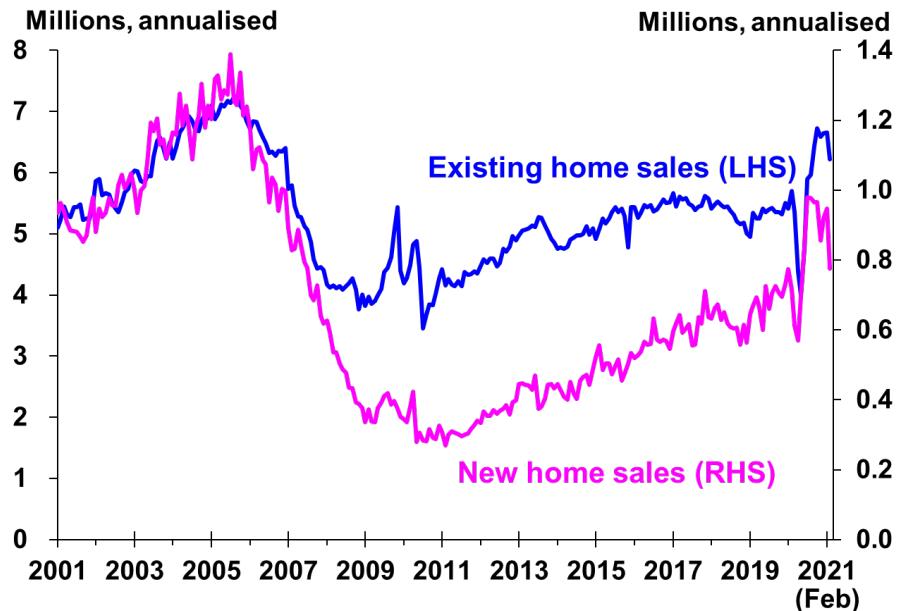
US: HOME PRICES



Sources: CEIC and Datastream



US: HOME SALES



Sources: CEIC and Datastream

13

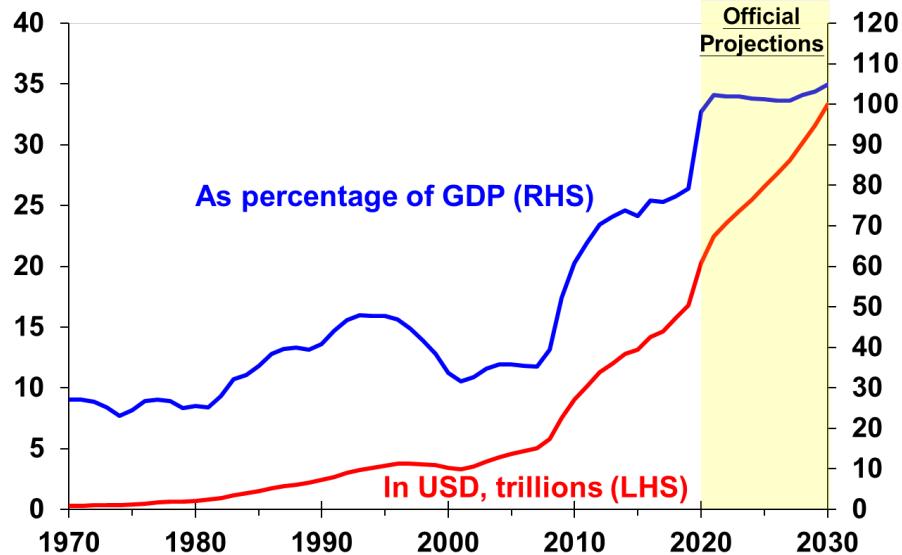


US: FEDERAL GOVERNMENT DEBT

US federal debt held by the public

USD, trillions

% of GDP



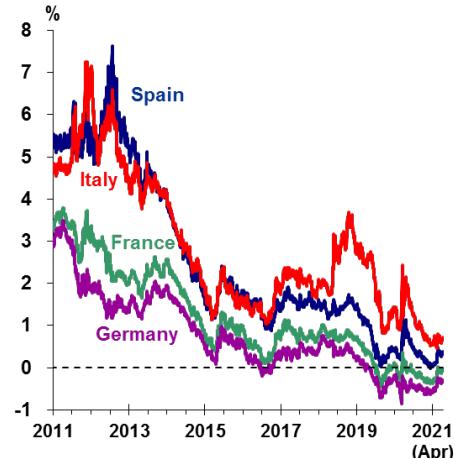
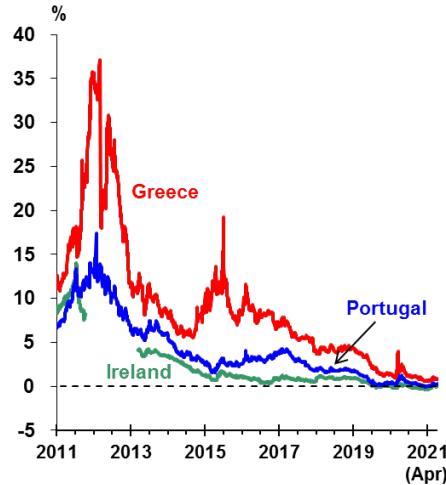
Sources: CEIC and Congressional Budget Office

14



EURO AREA: SOVEREIGN BOND YIELDS

10-year sovereign bond yield

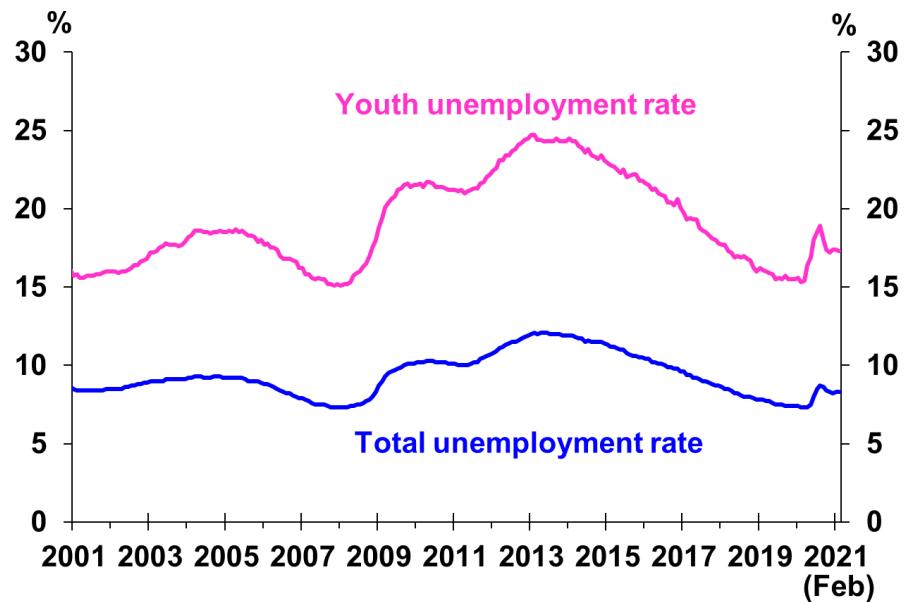


Note: 10-year Irish sovereign bond yield data is not available between 12 Oct 2011 and 14 Mar 2013

Source: Bloomberg



EURO AREA: UNEMPLOYMENT RATE

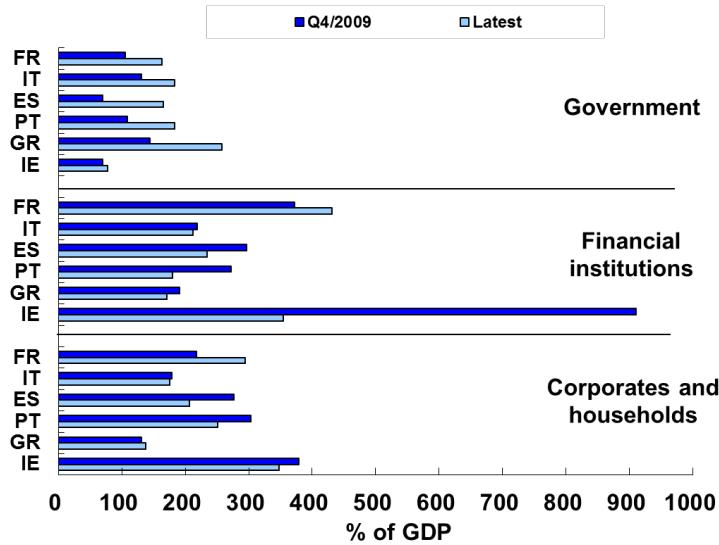


Source: Bloomberg

16



EURO AREA: OVERALL INDEBTEDNESS



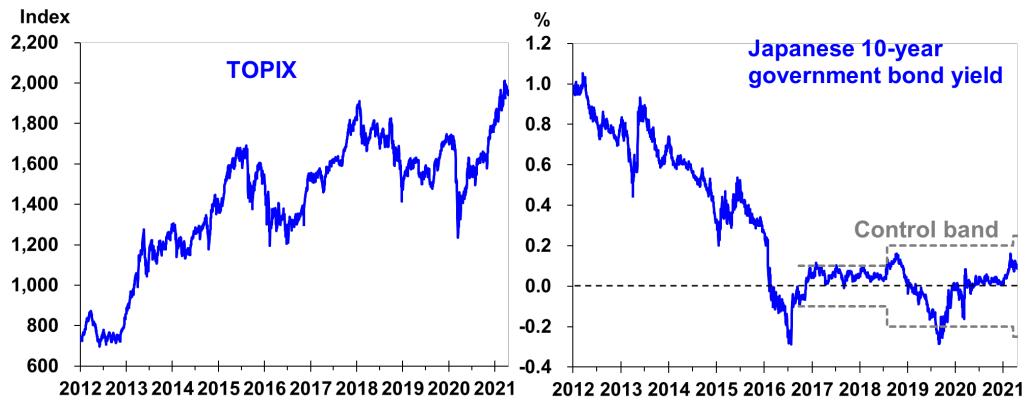
Source: European Central Bank

Note: FR – France, IT – Italy, ES – Spain, PT – Portugal, GR – Greece, IE – Ireland

The latest figures are up to Q4/2020 for financial institutions, whilst the rest are up to Q3/2020



JAPAN: FINANCIAL MARKETS



Source: Bloomberg

18



JAPAN: PUBLIC DEBT

% of GDP

300

250

200

150

100

2000

2004

2008

2012

2016

2020

(Dec)

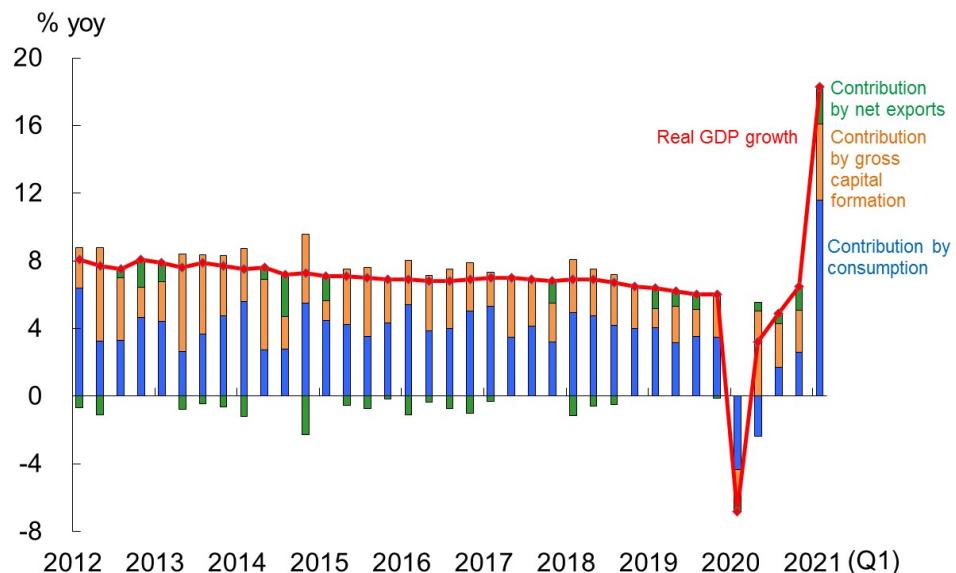
Public debt

Sources: Bank of Japan and CEIC

19



MAINLAND CHINA: REAL GDP GROWTH

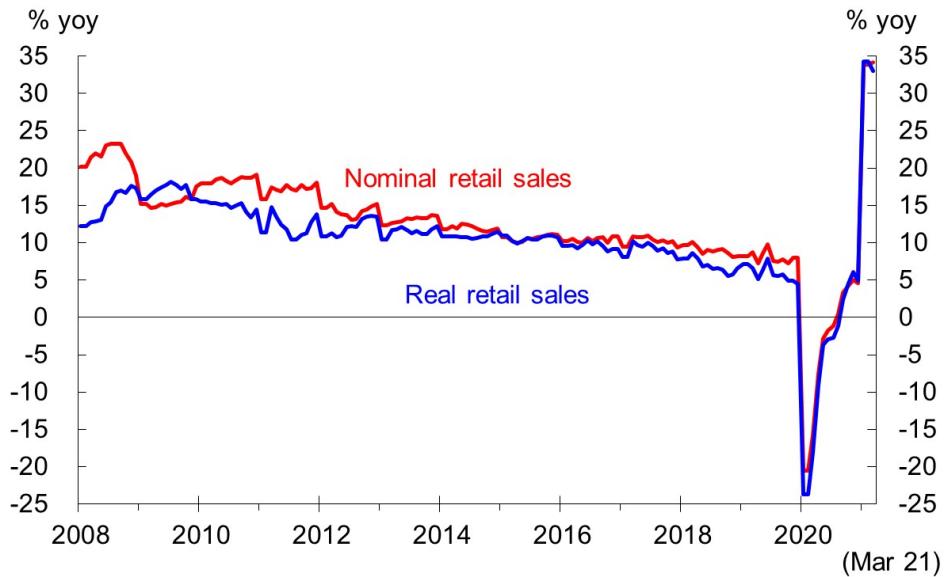


Source: CEIC

20



MAINLAND CHINA: RETAIL SALES



Note: January and February figures are the average annual growth rate for the first two months of the year
Sources: WIND and HKMA staff estimates



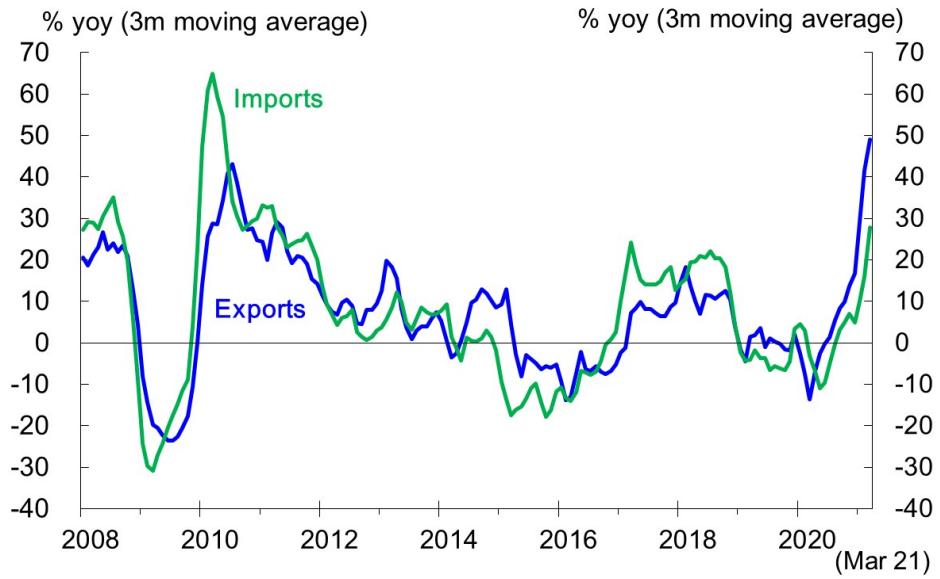
MAINLAND CHINA: FIXED ASSET INVESTMENT



Sources: CEIC and HKMA staff estimates



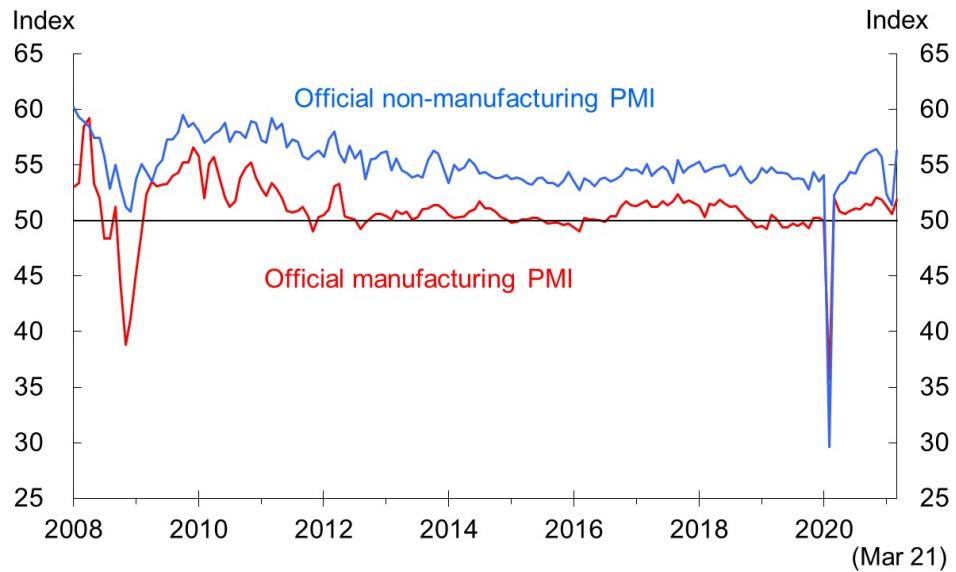
MAINLAND CHINA: IMPORT AND EXPORT GROWTH



Sources: CEIC and HKMA staff estimates



MAINLAND CHINA: PURCHASING MANAGERS' INDEX

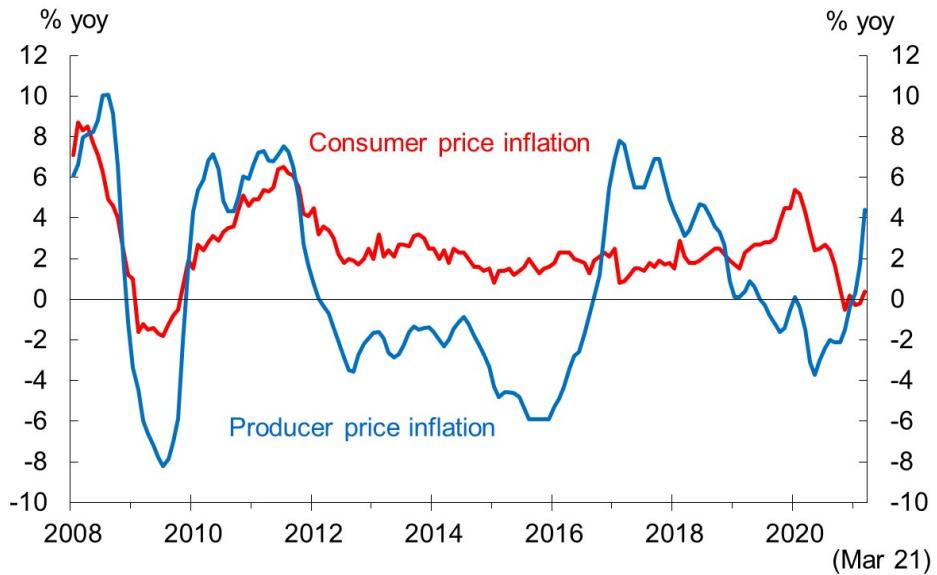


Source: CEIC

24



MAINLAND CHINA: INFLATION

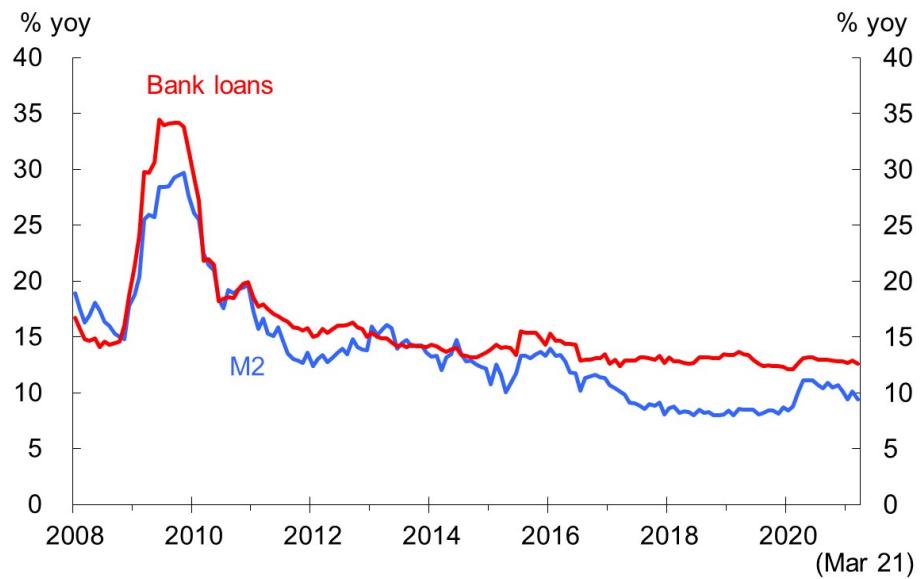


Source: CEIC

25



MAINLAND CHINA: MONEY AND LOAN GROWTH

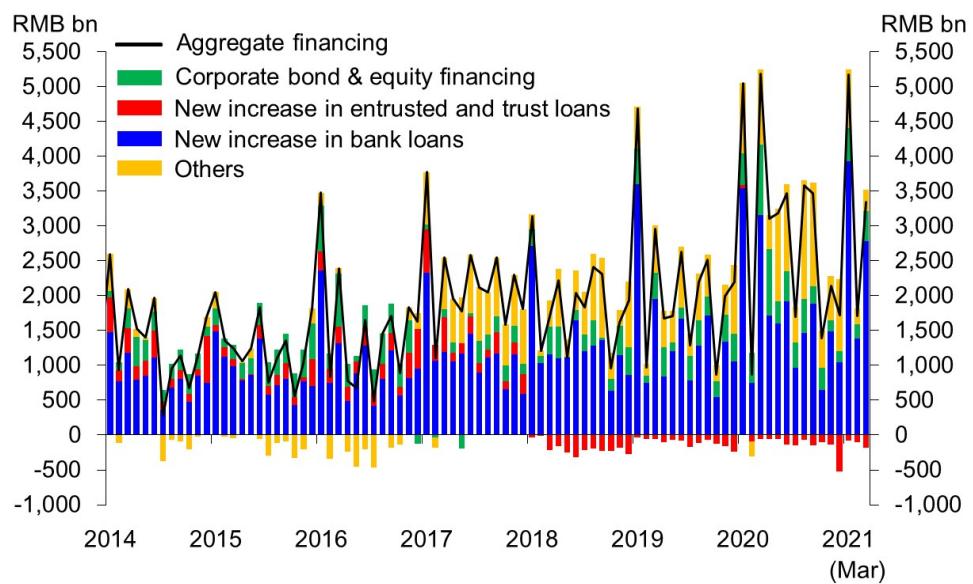


Source: CEIC

26



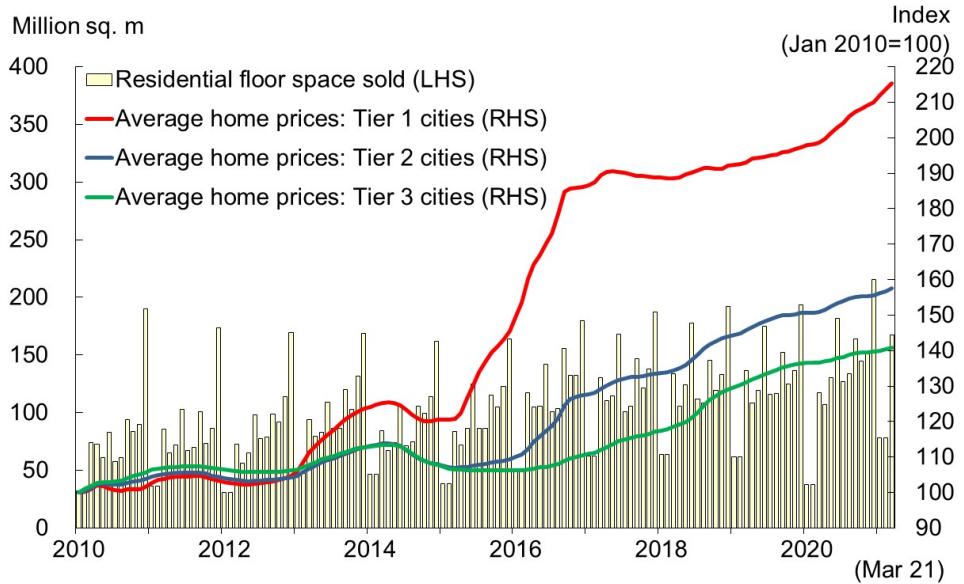
MAINLAND CHINA: AGGREGATE FINANCING FLOW



Source: CEIC



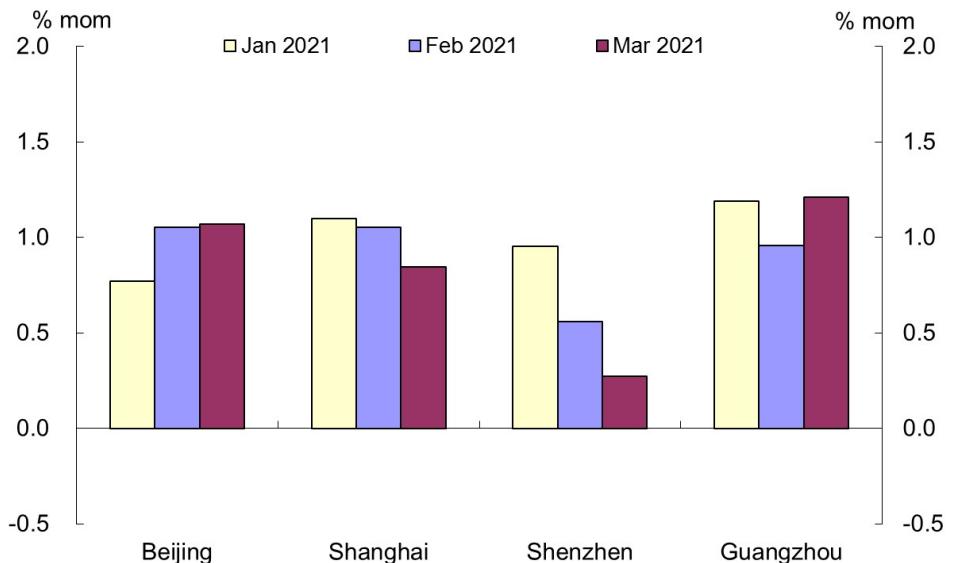
MAINLAND CHINA: PROPERTY PRICE AND TRANSACTION VOLUME



Sources: CEIC and HKMA staff estimates



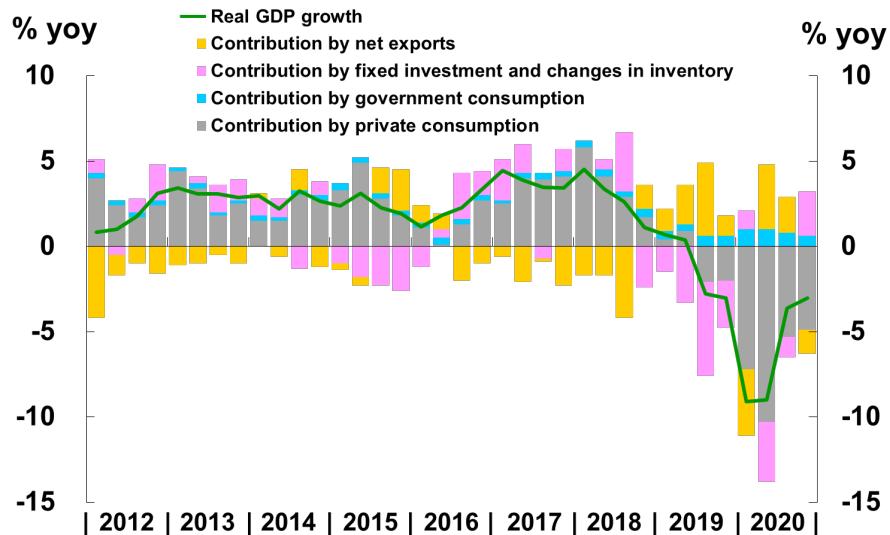
MAINLAND CHINA: HOUSING PRICE CHANGES IN MAJOR CITIES



Sources: CEIC, WIND and HKMA staff estimates



HONG KONG: REAL GDP GROWTH

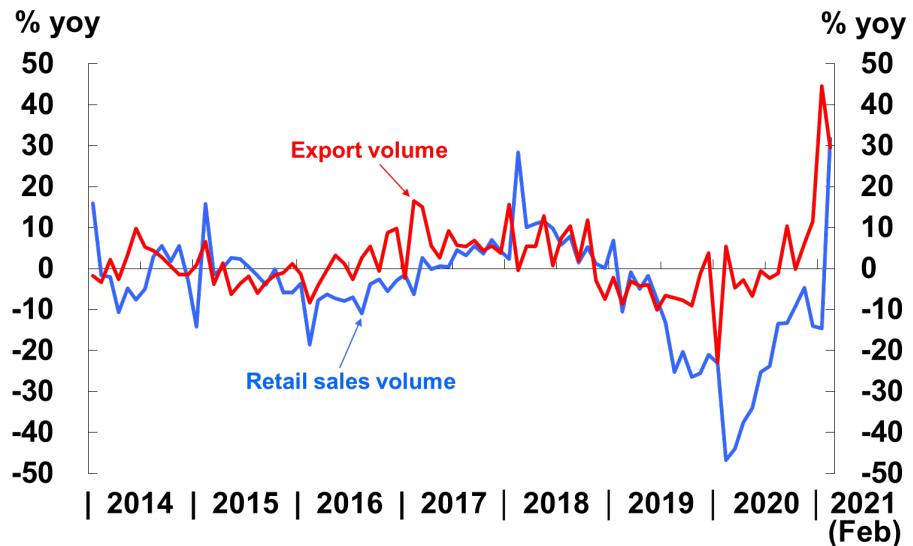


Source: C&SD

30



HONG KONG: ECONOMIC ACTIVITY

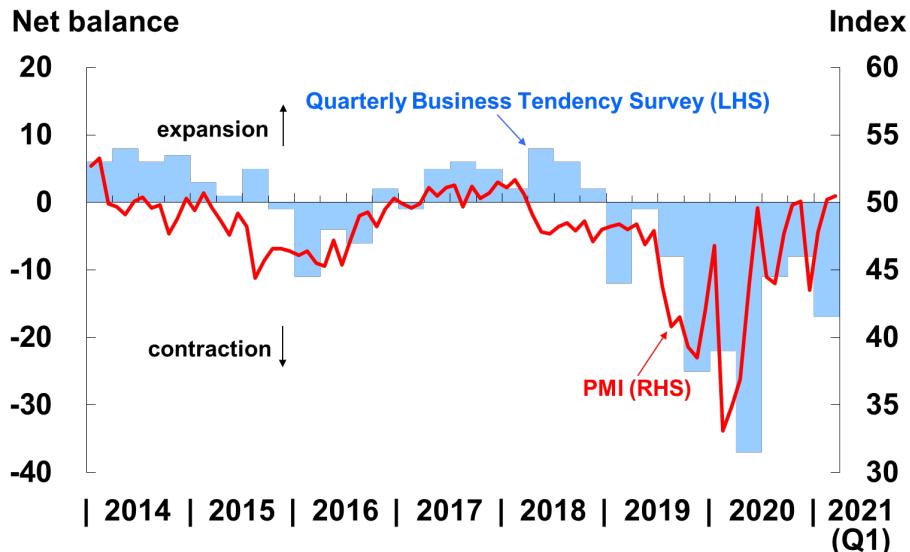


Source: C&SD

31



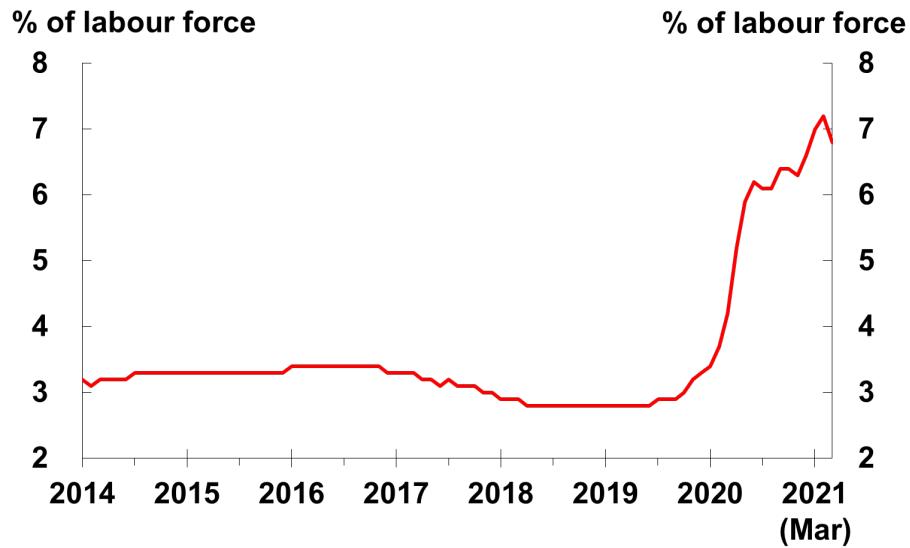
HONG KONG: BUSINESS OUTLOOK



Sources: C&SD and IHS Markit



HONG KONG: UNEMPLOYMENT RATE

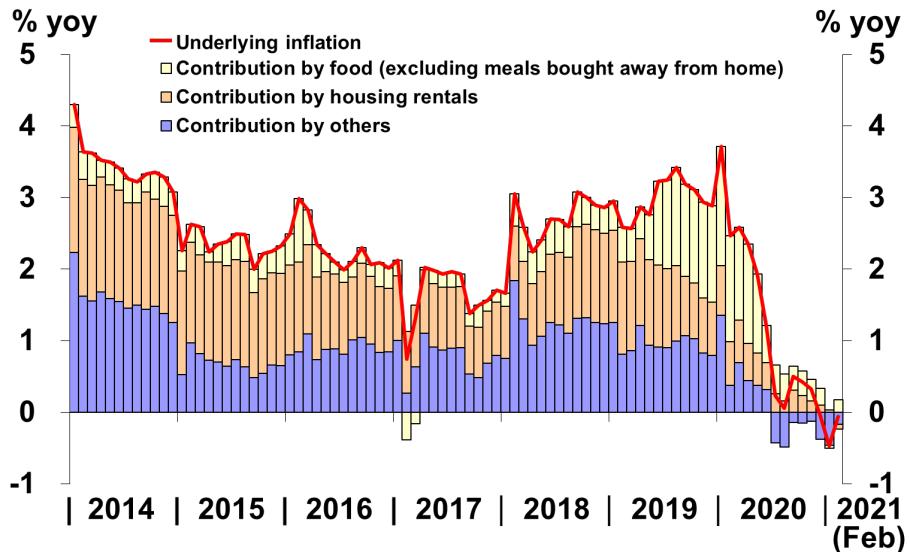


Source: C&SD

33



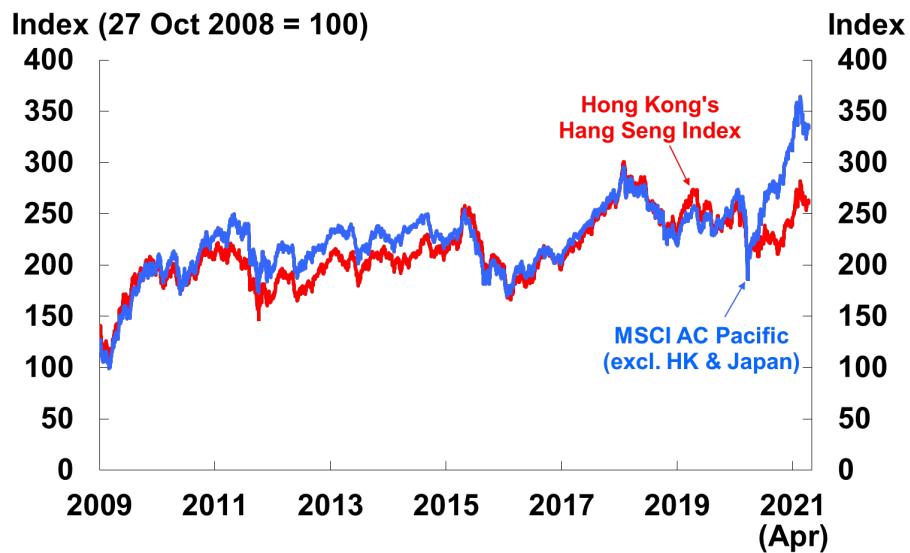
HONG KONG: INFLATION



Sources: C&SD and HKMA staff estimates



HONG KONG: EQUITY MARKET

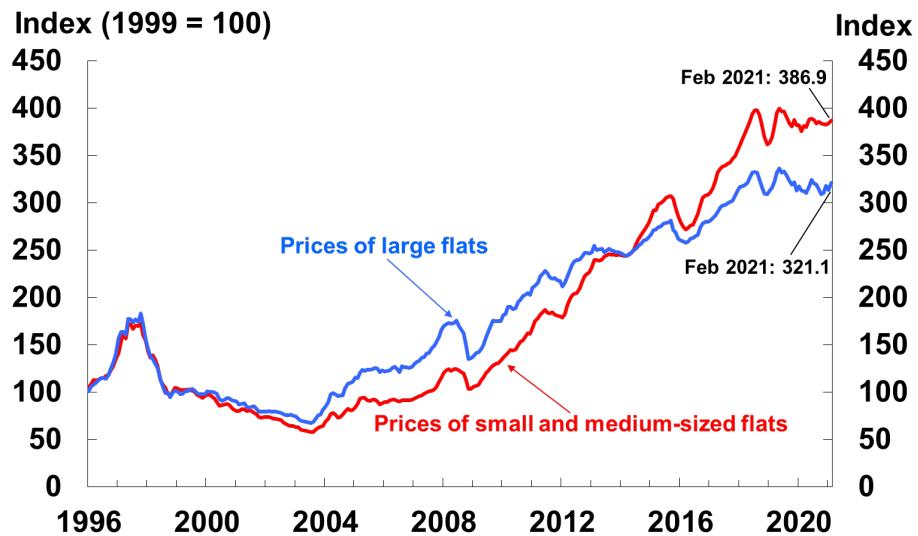


Source: Bloomberg

35



HONG KONG: RESIDENTIAL PROPERTY PRICES



Source: Rating and Valuation Department



HONG KONG: TRANSACTION VOLUME IN THE PRIMARY AND SECONDARY MARKETS

Transactions (in thousands)

18
16
14
12
10
8
6
4
2
0

Primary market
Secondary market

2009 2011 2013 2015 2017 2019 2021
(Mar)

Transactions (in thousands)

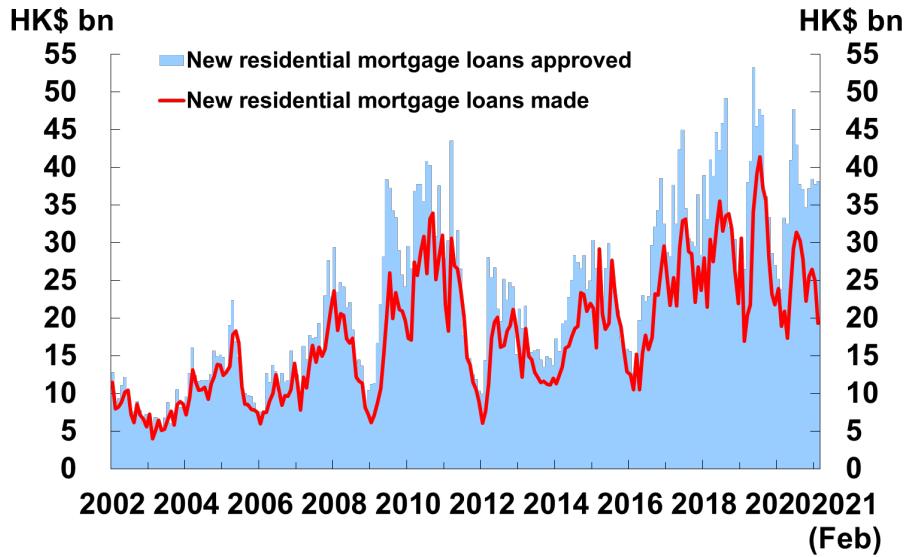
18
16
14
12
10
8
6
4
2
0

Source: The Land Registry

37



HONG KONG: NEW RESIDENTIAL MORTGAGE LOANS



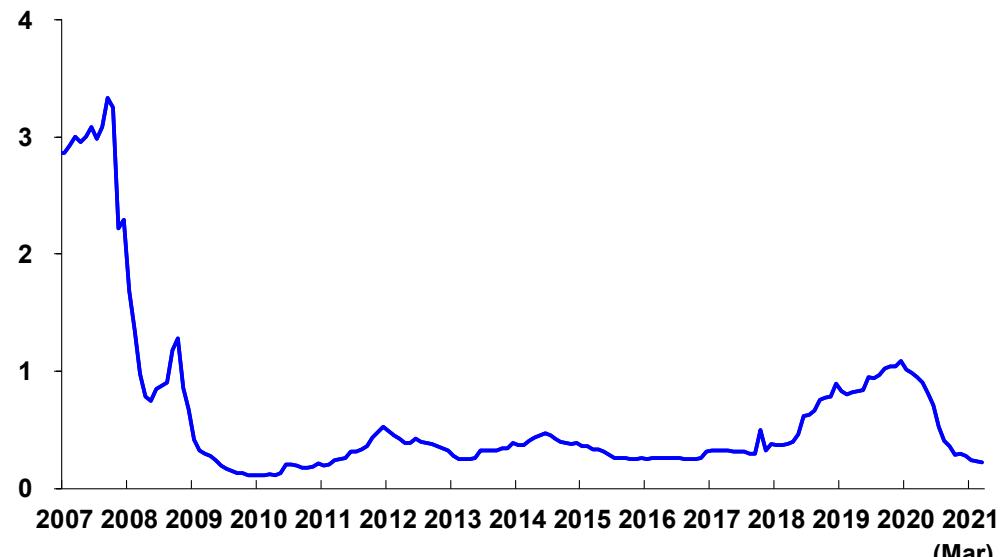
Source: HKMA

38



HONG KONG: COMPOSITE INTEREST RATE

% p.a.

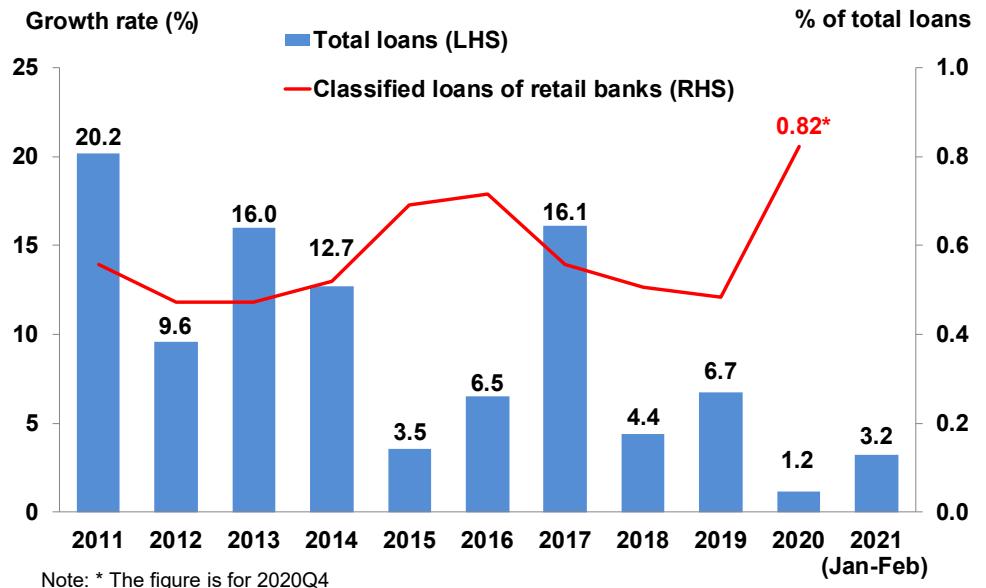


Source: HKMA

(Mar)
39



HONG KONG: LOAN GROWTH AND ASSET QUALITY



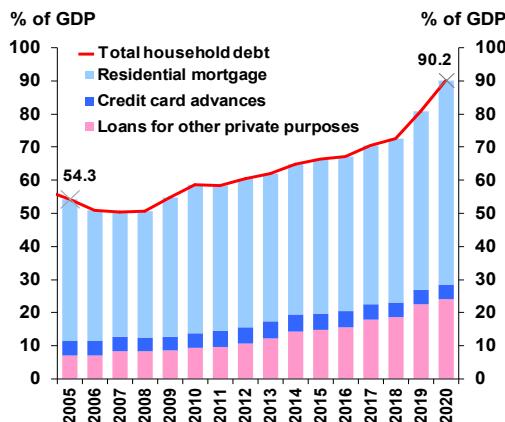
Source: HKMA

40

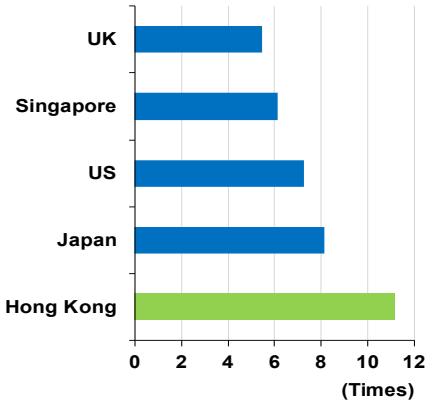


HONG KONG: HOUSEHOLD DEBT

Gross household debt



Household net worth-to-liabilities ratio



Notes: (1) Household net worth (or net household assets) is the difference between gross household assets and gross household liabilities. (2)The Japan figure is from end-2018, while the figures for the other economies are from end-2019.

Sources: HKMA staff estimates, and statistical agencies or central banks of selected economies.

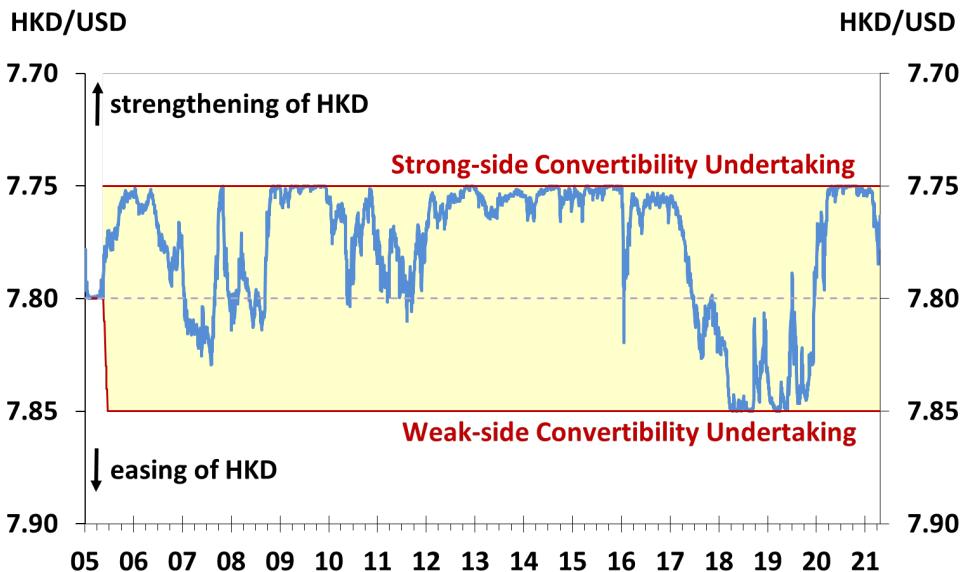
Source: HKMA



CURRENCY STABILITY



HONG KONG DOLLAR SPOT EXCHANGE RATE





AGGREGATE BALANCE

HK\$ billion

500

450

400

350

300

250

200

150

100

50

0

2015

2016

2017

2018

2019

2020

2021

HK\$ billion

500

450

400

350

300

250

200

150

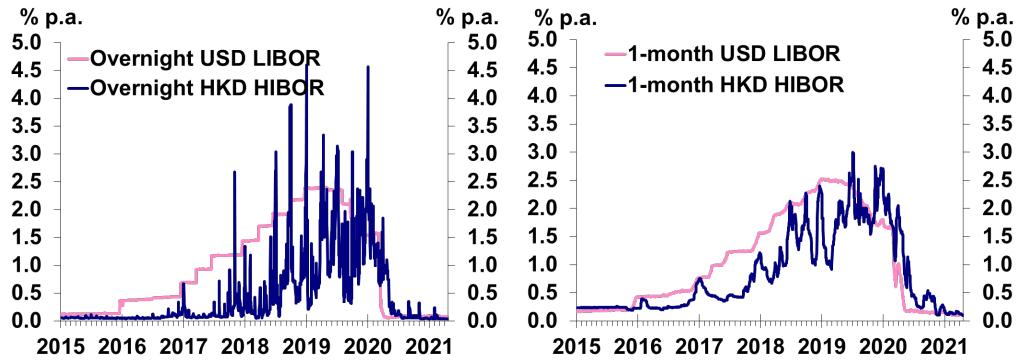
100

50

0



DOMESTIC INTEREST RATES





12-MONTH HONG KONG DOLLAR FORWARD POINTS



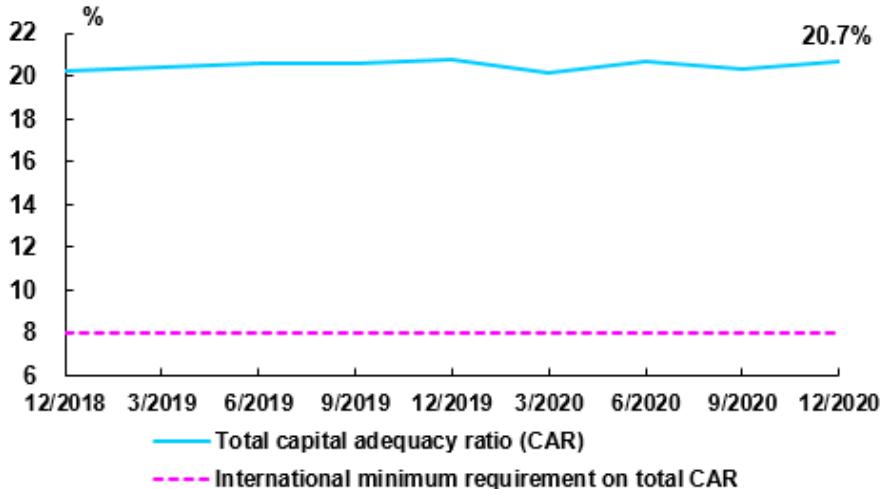


BANKING STABILITY



BANKING SECTOR PERFORMANCE

Locally incorporated authorized institutions (AIs) stayed well capitalised



Source: HKMA

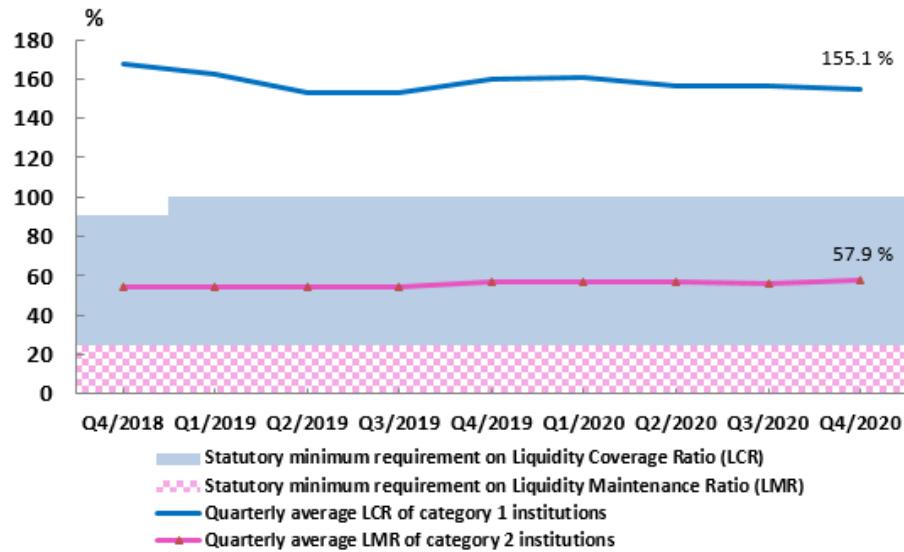
48

- The banking sector remained well capitalised. The total CAR of locally incorporated AIs stood at 20.7% at end-December 2020, well above the international minimum requirement of 8%.



BANKING SECTOR PERFORMANCE

Liquidity position remained sound



Source: HKMA

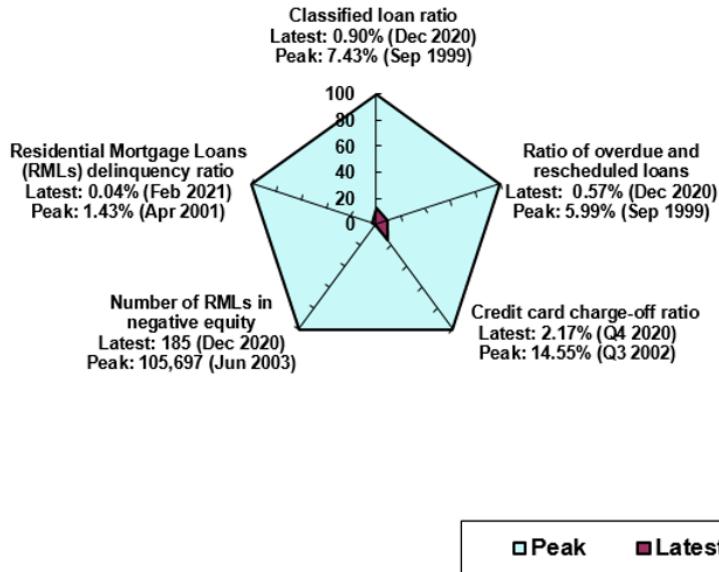
49

- In the fourth quarter of 2020, the quarterly average LCR of category 1 institutions was 155.1%, well above the statutory minimum requirement of 100%. For category 2 institutions, their quarterly average LMR was 57.9%, also well above the statutory minimum requirement of 25%.



BANKING SECTOR PERFORMANCE

Asset quality remained at healthy levels



Source: HKMA

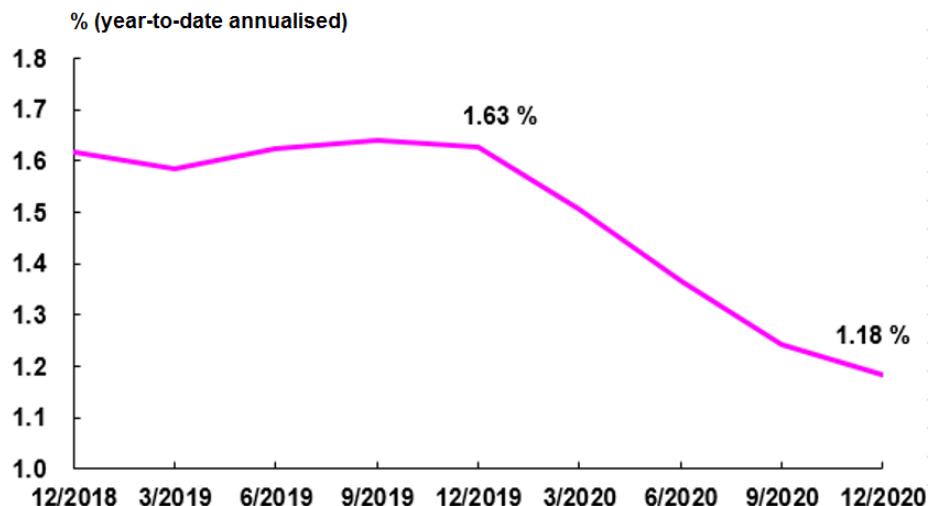
50

- As COVID-19 persists, the asset quality of the banking sector deteriorated slightly but remained at healthy levels. The classified loan ratio of the banking sector increased to 0.90% at end-December 2020 from 0.84% a quarter earlier. It was significantly below the long-term average of 1.8% since 2000.



BANKING SECTOR PERFORMANCE

Net interest margin (NIM) narrowed



Source: HKMA

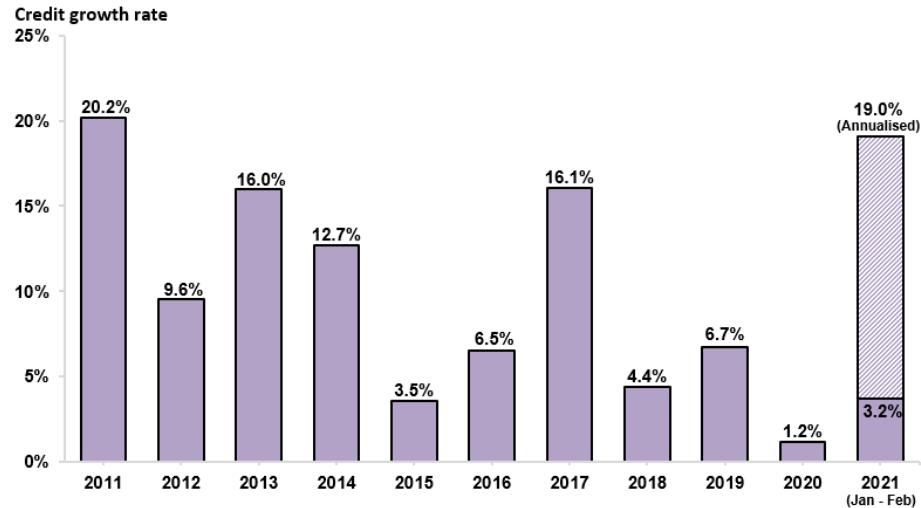
51

- The NIM of retail banks' Hong Kong offices narrowed to 1.18% in 2020 from 1.63% in 2019. This was due to a general decline in interest rates starting in the second quarter of 2020.



BANKING SECTOR PERFORMANCE

Credit grew because of IPO activities



Source: HKMA

52

- Total loans increased by 3.2% in the first two months of 2021, partly driven by initial public offering (IPO) loans. Excluding the IPO loans, total loans would have grown by 1.7% during the period, or 10.3% on an annualised basis.



FIGHTING THE VIRUS AND SUPPORTING THE ECONOMY

Extended Pre-approved Principal Payment Holiday Scheme

- As announced in March, principal payments of eligible small and medium-sized enterprises to be deferred by another six months till October 2021
- Aggregate number of cases involving credit relief (up to February 2021):
 - Corporate customers: 60,000 cases (HK\$760 billion)
 - Individual customers: 31,000 cases (HK\$45 billion)

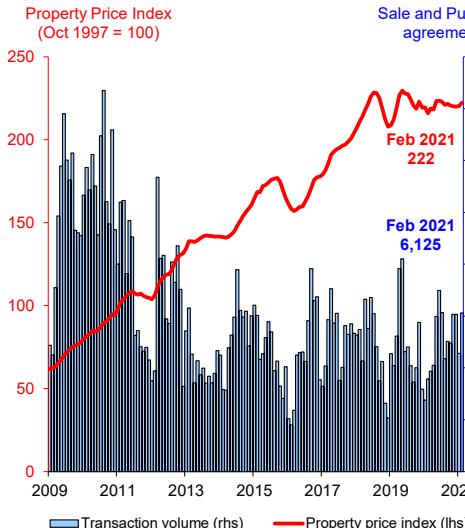
Enhanced SME Financing Guarantee Scheme

- Enhanced the Special 100% Loan Guarantee Scheme
- Principal moratorium for 80% and 90% Guarantee Products deferred till end-2021



PROPERTY MORTGAGE LOANS (RMLs)

Residential property price index and transaction volume



Average loan-to-value (LTV) ratio and debt servicing ratio (DSR) for newly approved residential mortgage loans



Sources: R&VD and Land Registry

54

- The average LTV ratio of newly approved RMLs hovered at 58% recently, following a rise in the earlier period, primarily driven by a larger proportion of RMLs with mortgage insurance which generally have a higher LTV ratio. The HKMA considers the risk manageable as the portion of loans above the HKMA's permissible LTV cap is covered by mortgage insurance.

Latest statistics on RMLs

	Monthly average in 2019	Monthly average in 2020	Sep 2020	Oct 2020	Nov 2020	Dec 2020	Jan 2021	Feb 2021
Number of sale and purchase agreements	4,983	4,990	5,024	4,951	6,070	6,067	4,562	6,125
Number of new RML applications	12,244	11,709	12,288	10,908	11,375	11,396	13,112	12,455
Number of new RMLs approved	8,981	7,763	7,826	7,311	7,986	8,039	8,073	7,926

Latest statistics on residential property prices

Property price index		Period	Property price index
Rating and Valuation Department (10/1997=100)	Latest position	2/2021	2/2021
	Recent peak	5/2019	5/2019
	Peak in 1997	10/1997	10/1997
Centaline (6/7/1997=100)	Latest position	11/4/2021	11/4/2021
	Recent peak	30/6/2019	30/6/2019
	Peak in 1997	19/10/1997	19/10/1997



INTERNATIONAL STANDARDS IMPLEMENTATION

2021

- Amendments to Banking (Capital) Rules – revised capital treatment on banks' equity investments in funds
- Amendments to Banking (Exposure Limits) Rules – technical refinements

2022

- Amendments to Banking (Capital) Rules – Basel III final reform package

55

Preparatory work for legislative amendments to implement the Basel regulatory standards is progressing:

Year 2021

Targeted to be submitted to LegCo sometime in 2021 (potentially sometime in second half of the year) are:

- amendments to the Banking (Capital) Rules to reflect the revised Basel capital requirement on banks' exposures to equity investments in funds; and
- amendments to the Banking (Exposure Limits) Rules to incorporate certain technical refinements to enhance clarity and better reflect the policy intent of certain existing provisions.

Year 2022

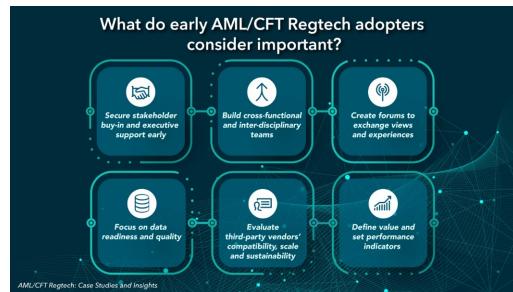
The above will be followed sometime in 2022 with the submission of amendments to the Banking (Capital) Rules to implement two sets of capital standards under the Basel III reforms. These consist respectively of:

- revisions to the credit risk, operational risk, and leverage ratio frameworks, as well as requirements for the prudent use of internal models (which are scheduled to take effect from 2023 as minimum standards for banks); and
- a revised market risk framework which is scheduled to take effect from 2023 for reporting purposes by locally incorporated AIs (and no earlier than that for the actual capital requirements).



ANTI-MONEY LAUNDERING

- Published “*AML/CFT Regtech: Case Studies and Insights*” in January 2021
 - First time to share comprehensive and practical, hands-on experience from banks that have actually implemented Anti-Money Laundering and Counter-Financing of Terrorism (AML/CFT) Regtech
 - Thematic insights designed to help banks to identify an adoption process that is applicable to their particular circumstances



56

- The HKMA published the report “*AML/CFT Regtech: Case Studies and Insights*”, which forms part of our ongoing initiative to promote Regtech adoption in AML/CFT work in the banking sector, building on the significant progress made since the first AML/CFT Regtech Forum hosted by the HKMA in November 2019.
- This is the first time that we studied and shared comprehensive and practical, hands-on experience as well as success stories from the AML/CFT Regtech adoption journeys of banks of different sizes and business scopes. The examples provide sufficient details and the thematic insights will help banks to identify an adoption process that is applicable to their particular circumstances.
- The HKMA encourages banks to draw reference from the examples and insights that are relevant to their particular circumstances to inform the appropriate Regtech adoption journey. This will also form the basis for our ongoing engagement with the industry throughout 2021 across a number of themes.



RESOLUTION REGIME

- Rules to be made under the Financial Institutions (Resolution) Ordinance (FIRO) on contractual stays (Stay Rules) requiring a provision in certain financial contracts to recognise any suspension of termination rights imposed by the Monetary Authority under the FIRO
- Industry consultation on draft text of the Stay Rules closed in January 2021. The plan is to introduce the Stay Rules into the LegCo for negative vetting in the current Legislative Session

57

- The Stay Rules to be made by the Monetary Authority as a resolution authority under the FIRO require Hong Kong incorporated AIs and some of their group companies to include a provision in certain financial contracts that are not governed by Hong Kong law so that the parties to the contracts agree to be bound by a suspension of termination rights (i.e. “stay”) that may be imposed by the Monetary Authority under the Hong Kong resolution regime. The Stay Rules are intended to implement the relevant Financial Stability Board principles for enhancing the effectiveness of cross-border resolution actions.
- Following public consultation on the policy proposals, the industry was consulted on draft text of the Stay Rules. The plan is to introduce the Stay Rules into the LegCo for negative vetting in the current Legislative Session.



FINANCIAL INCLUSION

- Continue to work closely with the banking industry and stakeholders to develop industry guideline on banking services for customers in need
- Continued uptake of Simple Bank Accounts (SBAs) service by small and medium-sized enterprises

58

- The HKMA continues to work closely with the banking industry and other relevant stakeholders to develop industry guideline on providing services to customers in need with a view to further promoting financial inclusion. Moreover, the HKMA monitors the implementation by banks on the two published industry guidelines, i.e. the “Practical Guideline on Barrier-free Banking Services” in March 2018 and the “Guideline on Banking Services for Persons with Intellectual Disabilities” in December 2020. Banks are making good progress in the implementation of these guidelines so far.
- The HKMA continues encouraging banks to support and launch SBA service to provide basic banking services with less extensive customer due diligence measures, hence offering more choices to corporate customers. As of February 2021, there are four banks offering such service with over 6,400 SBA accounts opened.



BANKING CONSUMER PROTECTION

- Commenced a Focused Review on Incentive Systems of Front Offices in Retail Banks
- Commenced a comprehensive review on the Code of Banking Practice to enhance customer protection in digitalised banking services
- Working closely with the Industry Associations to introduce more than one consumer Credit Reference Agency (CRA) – Industry Associations issued tenders in January. The new system is expected to be in operation by end-2022

59

- The HKMA issued a circular on 16 March 2021 to announce the commencement of a Focused Review on the incentive systems of front offices in sale and distribution of banking, investment and insurance products of 20 retail banks as part of the ongoing supervisory work of the HKMA to promote sound culture in the banking sector.
- In the light of the innovation and technology development of the banking industry and increasing use of digital banking services by consumers, the HKMA is committed to enhancing and strengthening consumer protection with respect to digital banking services. A comprehensive review of the Code of Banking Practice has been commenced in late last year with a view to: (1) providing effective protection to consumers in general and digital banking environments, including in areas like disclosure and transparency of important banking information to customers via digital means, business conduct of banks in digital channels, customers' awareness of financial risks in the digital environment, etc.; and (2) be in line with the latest international trend and best practices.
- The HKMA has been working closely with the Hong Kong Association of Banks, the Hong Kong Association of Restricted Licence Banks and Deposit-taking Companies and the Hong Kong S.A.R. Licensed Money Lenders Association Ltd. (collectively referred to as “Industry Associations”) to introduce more than one consumer CRA in Hong Kong. The HKMA seeks to implement the relevant arrangement soon with a view to enhancing the service quality of consumer CRAs and reducing the operational risk of having only one commercially-run consumer credit information service provider in the market, particularly the risk of single point of failure. The Industry Associations issued tenders for selection of CRAs on 29 January 2021. The new system is expected to be in operation by the end of 2022.



BANKING INVESTOR PROTECTION

- Followed up with banks on the implementation of refined investor protection measures
- Developing further guidance to banks on provision of investment and insurance services through non-face-to-face (non-F2F) channels
- Worked closely with the Insurance Authority to further extend the temporary facilitative measures for non-F2F sale of certain insurance products amid COVID-19
- Consulting the banking industry on a module of Supervisory Policy Manual (SPM) on supervision of insurance intermediary business of AIs

60

- The HKMA provided clarifications on individual authorized institutions' (AIs) enquiries to facilitate their implementation of the refined investor protection measures on the sale of investment, insurance and MPF products, following the issuance of Frequently Asked Questions to AIs in December 2020.
- There is an increasing use of non-F2F channels (e.g. online platforms) by AIs in the provision of investment and insurance services to customers. To ensure appropriate protection and customer friendly online journey to customers, the HKMA is developing further guidance to AIs on non-F2F provision of investment and insurance services. The guidance will focus on protection to vulnerable customers or customers lacking technology literacy, controls for suitability assessment, and product disclosure.
- Amid the uncertainties brought about by COVID-19, the HKMA and the Insurance Authority worked closely to further extend on 24 February the effective period of the phase 2 temporary facilitative measures for non-F2F sale of certain insurance products to until 30 June 2021. The scope of products covered (i.e. Qualifying Deferred Annuity Policy, Voluntary Health Insurance Scheme products, term insurance policies and certain refundable or renewable insurance policies that provide insurance protection) and the implementation details of measures remain unchanged.
- Following the implementation of the statutory regime under the Insurance Ordinance for insurance intermediaries, the HKMA plans to issue an SPM module on supervision of insurance intermediary business of AIs. The SPM module will outline the HKMA's supervisory approach and the relevant legal and regulatory requirements in relation to insurance regulated activities of AIs. The HKMA is consulting the banking industry.



PUBLIC EDUCATION

- Launched various initiatives, including well-received animated stickers, to encourage giving lai-see through electronic channels
- Enhanced education on traditional and social media to remind the public not to provide personal and account information via suspicious links in SMS/emails
- Co-organised an online quiz to enhance secondary school students' financial knowledge
- Through the HKMA's digital media channels
 - Promoted the HKMA's new initiatives in fintech and green finance
 - Addressed concerns about Hong Kong's status as an international financial centre



61

- The HKMA launched various initiatives, including a set of well-received animated stickers, before Chinese New Year to encourage the public to give lai-see through electronic channels, and to remind them of issues to note about exchanging new notes.
- In view of earlier fraud cases, the HKMA has stepped up efforts to remind the public to safeguard their personal digital keys, in particular not to provide personal and account information via suspicious links in dubious SMS/emails. Initiatives included customised social media posts, TV/radio APIs, online videos, and message dissemination in a radio programme and a webinar.
- Co-organised the “Hong Kong Financial Literacy Championship 2021” with various stakeholders to enhance secondary school students' financial knowledge. Response on the first phase in form of an online quiz was satisfactory.
- Through the HKMA's digital media channels:
 - Promoted the HKMA's new initiatives in fintech and green finance, including Global Regtech Challenge, m-CBDC Bridge and Government's issuance of green bonds; and
 - Shared facts and figures to address concerns about Hong Kong's status as an international financial centre.



DEPOSIT PROTECTION SCHEME (DPS)

- Entered final stage for introducing electronic payment channels for DPS compensation
- Organised webinars for Scheme members in respect of compliance with the information system requirements for compensation determination
- Launched two campaigns, “Manner Game King – Money-saving” and “DPS Love Story” via online/ offline media, and conducted various online DPS talks and workshops for promoting the awareness and understanding of DPS



62

- The Hong Kong Deposit Protection Board (the Board) is at the final stage of the project to introduce electronic payment channels for dispersing DPS compensation, including the Faster Payment System. Following training of payout agents, the Board is refining the system and procedures. The use of electronic payment channels will be ready in the second half of 2021.
- The Board organised information webinars with the aim of increasing awareness of Scheme members on compliance with the information requirements for payout of DPS compensation.
- Collaborated with two media partners in launching i) “Manner Game King – Money-saving” social media campaign to deliver DPS messages through Q&As in the form of popular online game show; and ii) “DPS Love Story” campaign to introduce DPS key features via dance and song on both digital and print media to reinforce public awareness and understanding of DPS protection.
- Continued to reach out to different target audience groups through online DPS talks and workshops:
 - Delivered talks to secondary schools to inculcate younger generation with the knowledge of DPS, money-management and saving;
 - Conducted talks for elderly centres and the Elder Academy to introduce the DPS; and
 - Collaborated with non-governmental organisations to conduct DPS board game introductory workshop for the children of low-income families to learn about saving and the DPS.



FINANCIAL INFRASTRUCTURE



FINANCIAL INFRASTRUCTURE

- Financial infrastructure remains safe and efficient
- Operation of Bond Connect has been smooth; actively promote Bond Connect to overseas investors
- Further refine the Hong Kong Trade Repository (HKTR) for over-the-counter derivatives according to the relevant local and international standards

64

Bond Connect

- Since the launch of Bond Connect on 3 July 2017, the related settlement operations performed by the Central Moneymarkets Unit have been smooth.
- With the Delivery-versus-Payment settlement fully implemented in August 2018, as well as the inclusion of renminbi-denominated Mainland government and policy bank securities into the Bloomberg Barclays Global Aggregate Index in April 2019 and J.P. Morgan Government Bond Index-Emerging Markets in February 2020, more overseas investors have started to invest in the Mainland interbank bond market via the Bond Connect. The HKMA has been maintaining close communications with the People's Bank of China and other relevant Mainland institutions to explore enhancements to Northbound Trading.

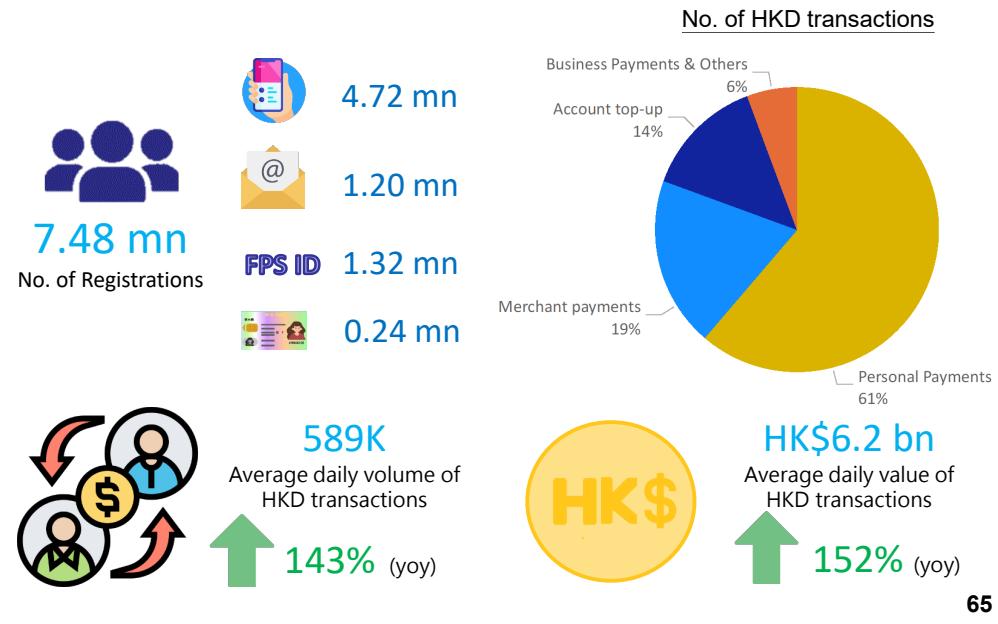
Over-the-counter derivatives trade repository

- Since the reporting function of the HKTR was launched in July 2013, reporting by banks to the HKTR has been smooth.



FASTER PAYMENT SYSTEM (FPS)

February 2021



65

- The number of registrations and turnover of the FPS have been growing steadily. Since the launch of the system till 28 February 2021, the FPS recorded 7.48 million registrations (including 4.72 million in mobile number, 1.2 million in email address, 1.32 million in FPS ID and 0.24 million in Hong Kong Identity number), up by 69% or 3.05 million registrations year-on-year.
- To facilitate institutions' payments to the general public, the FPS was enhanced to introduce the HKID number as an account proxy starting from 6 December 2020. This new function is not intended for making person-to-person payments. It will only be used by institutions which already possess the HKID number of the recipients of the payments. Banks will promote this service to their corporate customers, while the HKMA will also explore more use cases with the industry and the Government. Corporate customers generally take time to understand the new feature and need to upgrade their systems for application.
- The usage of FPS has expanded gradually to merchant payments and top-up transactions from primarily P2P transactions previously.
- The turnover of the FPS rose particularly fast amid the epidemic. The average daily Hong Kong dollar real-time transactions reached 589,000, amounting to HK\$6.2 billion in February 2021. Both the average daily volume and value rose over one time year-on-year.



LATEST FINTECH INITIATIVES

- In partnership with the Bank for International Settlements Innovation Hub (BISIH), expanded the Central Bank Digital Currency research project initiated by HKMA and Bank of Thailand, and included two additional central banking institutions:
 - Digital Currency Institute of the People's Bank of China (PBC DCI)
 - Central Bank of the United Arab Emirates (CBUAE)
- Launched Cross-border Testing (CBT) with the Global Financial Innovation Network (GFIN) and received 26 applications

66

- **Central Bank Digital Currency research for cross-border payments**

- In February 2021, the research project initiated by the HKMA and the Bank of Thailand was joined by the PBC DCI and the CBUAE. It is strongly supported by the BISIH Centre in Hong Kong.
- The project aims to foster a conducive environment for central banks in Asia and other regions to jointly study the potential of blockchain in enhancing the financial infrastructure for cross-border payments.
- In particular, it will explore the potential of blockchain in facilitating real-time cross-border foreign exchange payment-versus-payment transactions in a multi-jurisdictional and 24/7 context.

- **Cross-border Testing**

- Together with other members of the GFIN, the HKMA opened applications for the CBT between October and December 2020.
- The CBT provides an environment for firms to trial and scale new technologies, products or business models in multiple jurisdictions.



STORED VALUE FACILITIES (SVFs) AND RETAIL PAYMENT SYSTEMS (RPSs)

- SVF usage continued to grow in Q4 2020:
 - Accounts in use: 63.91 million (+1.2% year-on-year (oyy))
 - Average daily transaction value: HK\$660 million (+14.9% yoy)
 - Licensees continue to extend their business reach
- SVF Security 2.0:
 - Enhancements in SVF account structure and account opening process
 - Announced on 18 September 2020, and following up with SVF licensees on their progress of implementation
- Continue to supervise licensees in a risk-based manner, taking targeted supervisory actions where necessary
- Continue to oversee six designated RPSs



REGULATORY DEVELOPMENT OF THE OVER-THE-COUNTER (OTC) DERIVATIVES MARKET

- The HKMA and the Securities and Futures Commission (SFC) published a joint consultation paper in April 2021 to consult the market on the annual update to the Financial Services Providers (FSP) list for clearing obligations. A conclusion to the consultation is targeted to be published in June 2021 with a view to implementing the revised FSP list in January 2022
- As of March 2021, the Hong Kong Trade Repository logged a total of 2.98 million outstanding OTC derivatives trades, covering five asset classes under mandatory reporting requirements, i.e. foreign exchange, interest rate, equity, credit, and commodity derivatives

68

- Under the Hong Kong OTC Derivatives Clearing Rules (Clearing Rules), AIs and licensed corporations (LCs) are subject to the clearing obligation of specified OTC derivative transactions. In order to capture transactions between AIs/LCs and major dealers outside Hong Kong that are not AIs or LCs, the concept of FSP was introduced. Under the Clearing Rules, an entity will be designated as a FSP if the entity belongs to a firm on the Financial Stability Board's list of global systemically important banks or on the OTC Derivatives Supervisors Group's list of major dealers, and the entity is a clearing member of major central counterparties. Specific transactions between a FSP and AIs/LCs are subject to the clearing obligations. The HKMA and SFC perform annual review and public consultation of the FSP list to ensure the list remains relevant and appropriate.



INTEREST RATE BENCHMARK REFORMS

- The HKMA has been:
 - actively participating in discussion in international fora and closely monitoring relevant developments;
 - working with the Treasury Market Association to encourage the use of HONIA, gauging industry views and promoting market awareness; and
 - continuing to facilitate AIs in preparing for the discontinuation of LIBOR

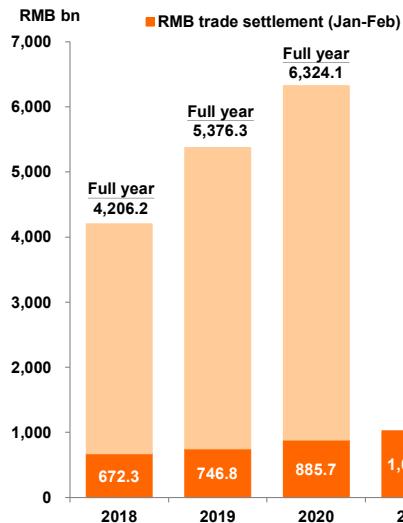


HONG KONG AS AN INTERNATIONAL FINANCIAL CENTRE

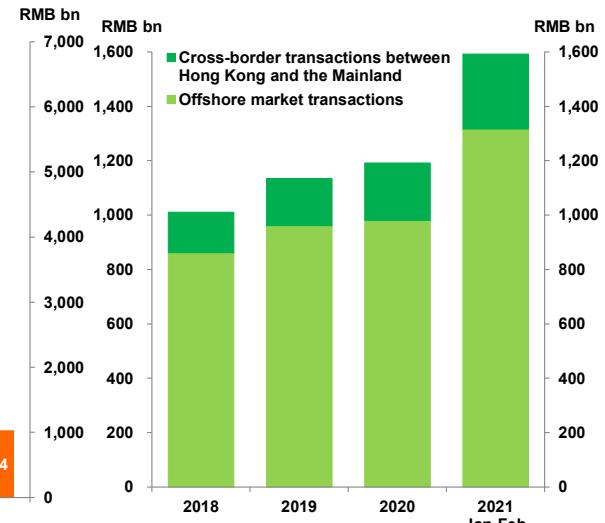


RMB TRADE SETTLEMENT AND PAYMENT

RMB trade settlement handled by banks in Hong Kong



Average daily turnover of Hong Kong RMB RTGS System



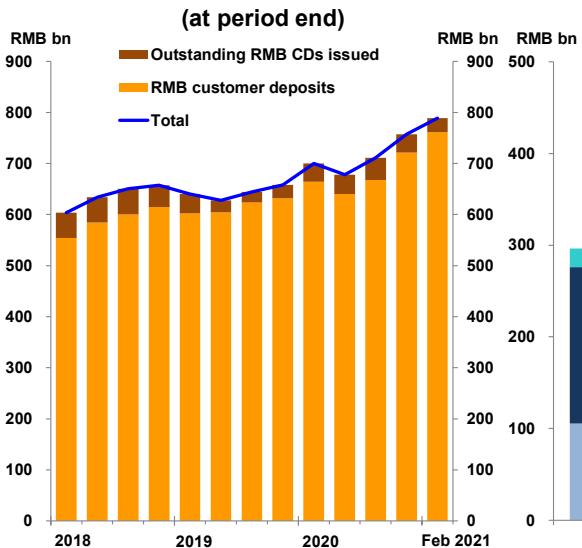
71

- In the first two months of 2021, renminbi trade settlement handled by banks in Hong Kong totalled RMB1,022.4 billion.
- In the first two months of 2021, the average daily turnover of Hong Kong RMB Real Time Gross Settlement (RTGS) system stood at RMB1,592.4 billion.

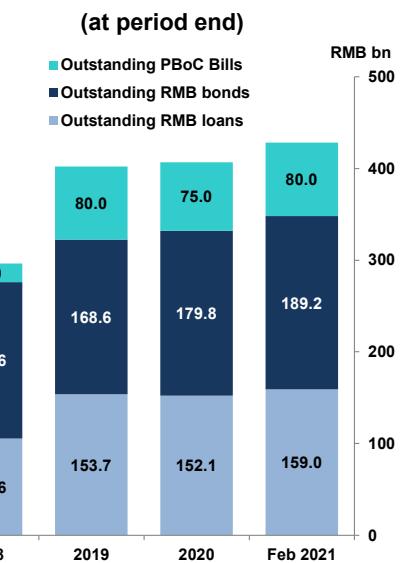


RMB LIQUIDITY POOL AND FINANCING ACTIVITIES

RMB customer deposits and RMB certificates of deposit (CDs)



RMB financing activities



72

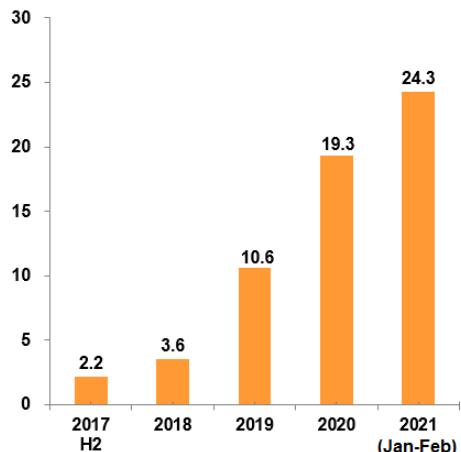
- As at end-February 2021, renminbi customer deposits and outstanding renminbi CDs amounted to RMB761.0 billion and RMB27.8 billion respectively, totalling RMB788.8 billion.
- As at end-February 2021, outstanding renminbi loans amounted to RMB159.0 billion. Outstanding dim sum bonds amounted to RMB189.2 billion. The dim sum bond issuance totalled RMB13.8 billion for the first two months of 2021. As at end-February 2021, outstanding PBoC bills amounted to RMB80 billion.



BOND CONNECT TURNOVER AND PARTICIPATING INSTITUTIONS

Average Daily Turnover

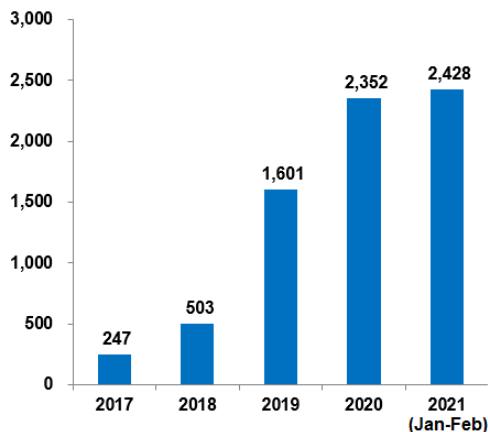
RMB bn



Number of Registered Institutional Investors

(at period end)

No. of Institutional Investors



73

- In the first two months of 2021, Bond Connect recorded 276 trades daily on average. The daily turnover averaged RMB24.3 billion, up around 26% from the 2020 average of RMB19.3 billion. As of end of February 2021, Bond Connect onboarded 2,428 registered institutional investors.



MAINTAINING RMB BUSINESS LINKS WITH OTHER JURISDICTIONS

	Feb 2021	2020	2019
1 No. of participating banks on Hong Kong's RMB clearing platform	207	206	204
Of which:			
Branches and subsidiaries of overseas banks and overseas presence of Mainland banks	172	172	173
2 Amount due to overseas banks (RMB billion)	151.1	99.4	76.3
3 Amount due from overseas banks (RMB billion)	116.3	97.3	95.4



DEVELOPING HONG KONG'S PRIVATE EQUITY (PE) PLATFORM

- Hong Kong has a robust PE industry: the total capital under management by PE funds in Hong Kong exceeded US\$170 billion at end-2020*
- A new limited partnership regime for PE funds came into operation on 31 August 2020. As at 22 March 2021, 154 funds had been registered under the new regime. The Government plans to submit a legislative proposal in Q2 2021 to allow foreign investment funds to re-domicile to Hong Kong
- The HKMA has also been working with the Administration on the legislative proposal to provide tax concession for PE carried interest. The relevant bill was introduced into the Legislative Council on 3 February 2021 and scrutinised by the Bills Committee on 9 March 2021

* Source: Asian Venture Capital Journal



PROMOTING GREEN FINANCE

- In December 2020, the Green and Sustainable Finance Cross Agency Steering Group (CASG), co-chaired by the HKMA and the Securities and Futures Commission, launched its green and sustainable finance strategy for Hong Kong and five key action points to promote green and sustainable finance in Hong Kong
- The HKMA successfully supported the Government in issuing US\$2.5 billion green bonds in February 2021, comprising 5-year, 10-year and 30-year tranches. The green bonds saw strong demand from investors, attracting orders more than five times the issuance size
- The HKMA is conducting preparatory work to assist the Government in expanding the scale and doubling the borrowing ceiling of the Government Green Bond Programme to HK\$200 billion to allow for further issuance of green bonds (include retail green bonds) totalling HK\$175.5 billion in the next five years, having regard to the market situation
- The Green and Sustainable Finance Grant Scheme is expected to commence operation in May to cover eligible bond issuers and loan borrowers' expenses on bond issuance and external review services. The Scheme will last for three years and the HKMA will be the administrator ⁷⁶

- The CASG aims to coordinate the management of climate and environmental risks to the financial sector, accelerate the growth of green and sustainable finance in Hong Kong and support the Government's climate strategies. Other members include the Environment Bureau, the Financial Services and the Treasury Bureau, the Hong Kong Exchanges and Clearing Limited, the Insurance Authority and the Mandatory Provident Fund Schemes Authority. The CASG launched its Strategic Plan that sets out six key focus areas (risk management, disclosure, capacity building, financial innovation, mainland opportunities, and collaboration) for strengthening Hong Kong's financial ecosystem to support a greener and more sustainable future in the longer term, and announced five nearer-term actions to address the most pressing issues:
 1. Mandate Climate-related disclosures aligned with the Task Force on Climate-related Financial Disclosures recommendations across relevant financial sectors no later than 2025;
 2. Aim to adopt the Common Ground Taxonomy jointly developed by Mainland China and European Union;
 3. Support the International Financial Reporting Standards Foundation's proposal to establish a new Sustainability Standards Board for developing and maintaining a global, uniform set of sustainability reporting standards;
 4. Promote climate-focused scenario analysis; and
 5. Establish a platform to act as a focal point for cross-sectoral capacity building, thought leadership and development of repository for green and sustainable finance resources.

- As announced in the 2021-22 Budget, upon the expiry of the Pilot Bond Grant Scheme and the Green Bond Grant Scheme in mid-2021, the two schemes will be consolidated into a Green and Sustainable Finance Grant Scheme.



HONG KONG ACADEMY OF FINANCE (AoF)

- **Financial Leadership Development** – Launched the Thematic Programme on Fintech and Digitalisation in April 2021 and continued organising conversation sessions with financial leaders
- **Research Activities** – the Hong Kong Institute for Monetary and Financial Research (HKIMR) released three new Applied Research papers in February 2021 and six new working papers on monetary and macroeconomic topics since the beginning of 2021

77

Financial Leadership Development

- The following virtual events were organised under the Leadership Development Programme:
 - Conversation sessions with Mr Ashley Alder, Chief Executive Officer of the Securities and Futures Commission on 29 January; Mr John Waldron, President and Chief Operating Officer of the Goldman Sachs Group on 9 March; Mr Laurence Fink (Larry Fink), Founder, Chairman and CEO of BlackRock on 13 April; Mr Ray Dalio, Founder, Co-Chairman and Co-Chief Investment Officer of Bridgewater Associates on 27 April.
 - The AoF's Thematic Programme on Fintech and Digitalisation has been rolled out in April, comprising four webinars of two hours each, to be conducted by leading industry experts and academics. The Programme covers artificial intelligence, machine learning, cryptography, algo-trading, RegTech, as well as their practical applications.

Research Activities

- In February 2021, three Applied Research papers exploring topics that are relevant to market participants and regulators in Hong Kong were released:
 - Do the Shades of Green Matter? The Pricing and Ownership of “Dark-green” Bonds (Professor Gianfranco Gianfrate, EDHEC Business School)
 - The Effect of a Closing Auction on Market Quality and Market Efficiency in the Stock Exchange of Hong Kong (Professor Chen Yao, The Chinese University of Hong Kong)
 - Doing Well by Doing Good? Risk, Return, and Environmental and Social Ratings (Professor Jeong Ho (John) Kim, Emory University)



INVESTMENT ENVIRONMENT AND PERFORMANCE OF THE EXCHANGE FUND

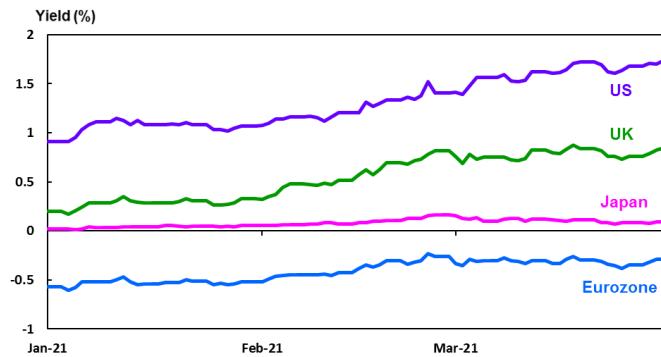


INVESTMENT ENVIRONMENT IN Q1 2021

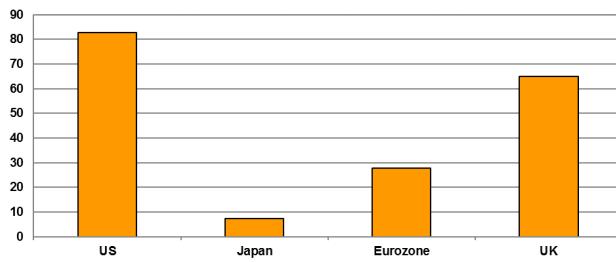
- **Interest rates:** Major sovereign bond yields rose in the first quarter amid rising inflation concerns and better growth outlook. US 10-year Treasury yield climbed to a 14-month high
- **Equity markets:** Major equity markets experienced correction against surging bond yields. Hang Seng Index fell after hitting two-year high within the quarter. With the progress of vaccine rollout and momentum of economic recovery, the US equity market pressed ahead after the adjustment, with the S&P 500 rebounding to record high
- **Exchange rates:** Major currencies showed mixed performance against the US dollar. Pound sterling appreciated while renminbi, euro and Japanese yen depreciated against the dollar during the quarter



MAJOR SOVEREIGN BOND YIELDS ROSE



2021 Q1 bond yield change (bps)

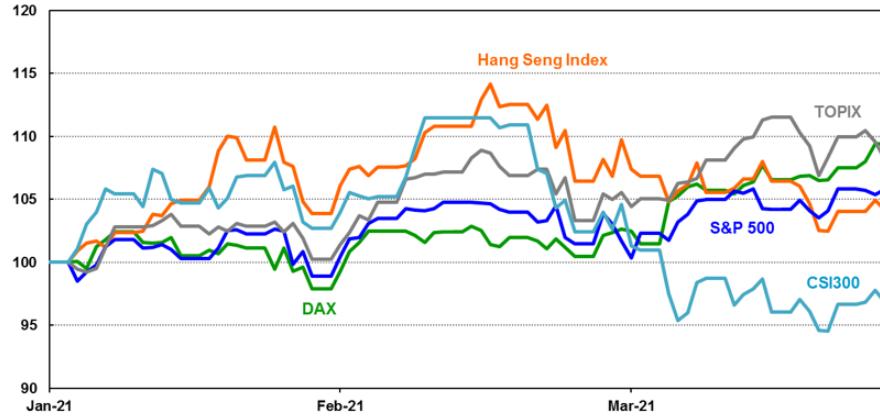


80



MAJOR EQUITY MARKETS EXPERIENCED CORRECTION

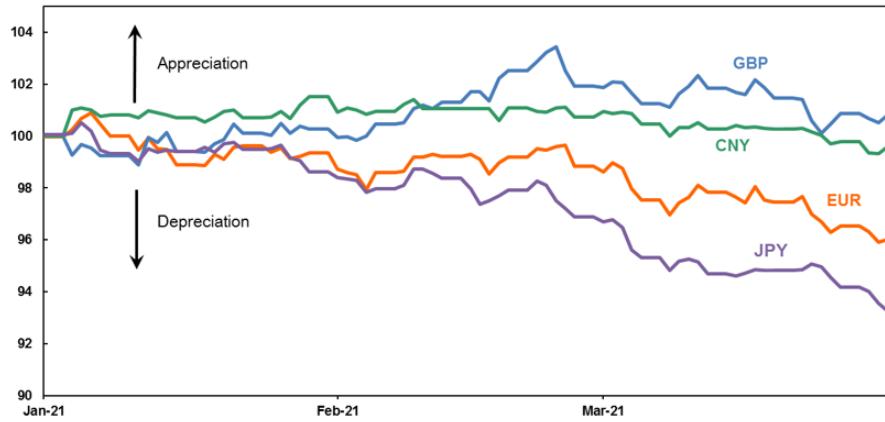
Normalised Index Level (2020 year-end = 100)





MAJOR CURRENCIES PERFORMED MIXED AGAINST USD

Normalised FX Level Against USD (2020 year-end = 100)





INVESTMENT INCOME

	2021 (unaudited)	2020	2019	2018
(HK\$ billion)	Q1	Full Year	Full Year	Full Year
Hong Kong equities*	7.6	4.0	22.1	(20.7)
Other equities	18.8	69.9	100.7	(38.7)
Bonds	(16.0)	92.7	114.5	57.4
Foreign exchange#	1.2	9.6	(13.0)	(9.0)
Other investments@	-	59.6	37.9	21.9
Investment income	11.6	235.8	262.2	10.9

* Excluding valuation changes of the Strategic Portfolio.

This is primarily the effect of translating foreign currency assets into Hong Kong dollar after deducting the portion for currency hedging.

@ Including valuation changes of private equity and real estate investments held under the Long-Term Growth Portfolio. Valuations of these investments for the first quarter of 2021 are not yet available.



INCOME AND EXPENDITURE

	2021 (unaudited)	2020	2019	2018
(HK\$ billion)	Q1	Full Year	Full Year	Full Year
Investment income	11.6	235.8	262.2	10.9
Other income	-	0.2	0.2	0.2
Interest and other expenses	(1.3)	(14.6)	(24.8)	(17.9)
Net income/(loss)	10.3	221.4	237.6	(6.8)
Fee payment to Fiscal Reserves*#	(9.2)	(69.8)	(53.8)	(60.2)
Fee payment to HKSAR government funds and statutory bodies*	(3.9)	(11.5)	(9.0)	(13.8)

* The rate of fee payment is 4.7% for 2021, 3.7% for 2020, 2.9% for 2019 and 4.6% for 2018.

This does not include the 2021 fee payment to the Future Fund because such amount will only be disclosed when the composite rate for 2021 is available.

(The composite rate was 12.3% for 2020, 8.7% for 2019 and 6.1% for 2018. Fee payable to the Future Fund was HK\$37.2 billion for 2020, HK\$24.4 billion for 2019 and HK\$16.4 billion for 2018.)



EXCHANGE FUND ABRIDGED BALANCE SHEET

(HK\$ billion)

ASSETS

	At 31 Mar 2021 (Unaudited)	At 31 Dec 2020	At 31 Dec 2019	At 31 Dec 2018
Deposits	280.0	267.0	305.9	325.7
Debt securities	3,249.9	3,238.0	2,856.6	2,825.2
Hong Kong equities*	216.4	206.9	194.8	175.5
Other equities	542.4	536.3	534.9	452.3
Other assets#	<u>247.0</u>	<u>251.0</u>	<u>314.5</u>	<u>276.2</u>
Total assets	4,535.7	4,499.2	4,206.7	4,054.9
LIABILITIES AND EQUITY				
Certificates of Indebtedness	567.2	556.2	516.1	485.7
Government-issued currency notes and coins in circulation	13.1	12.8	13.0	12.6
Balance of the banking system	457.5	457.5	67.7	78.6
Exchange Fund Bills and Notes issued	1,068.7	1,068.9	1,152.3	1,129.6
Placements by banks and other financial institutions	63.1	87.6	35.0	56.3
Placements by Fiscal Reserves	926.2	881.8	1,137.5	1,173.5
Placements by HKSAR government funds and statutory bodies	343.6	342.5	328.4	320.6
Placements by subsidiaries	16.2	15.5	12.6	7.7
Other liabilities	<u>246.5</u>	<u>233.1</u>	<u>194.7</u>	<u>180.0</u>
Total liabilities	3,702.1	3,655.9	3,457.3	3,444.6
Accumulated Surplus	832.7	842.4	748.7	609.7
Revaluation Reserve	<u>0.9</u>	<u>0.9</u>	<u>0.7</u>	<u>0.6</u>
Total equity	833.6	843.3	749.4	610.3
Total liabilities and equity	4,535.7	4,499.2	4,206.7	4,054.9

* Including shares of the Hong Kong Exchanges and Clearing Limited in the Strategic Portfolio.

Including fund injection to Exchange Fund's investment holding subsidiaries at a carrying amount of HK\$195.0 billion at 31 March 2021 (HK\$193.2 billion at 31 December 2020, HK\$177.3 billion at 31 December 2019 and HK\$162.4 billion at 31 December 2018).



HISTORICAL INVESTMENT INCOME

(HK\$ billion)

Year	Full Year	Q4	Q3	Q2	Q1
2002	47.0	26.3	(2.1)	26.5	(3.7)
2003	89.7	33.5	8.4	41.1	6.7
2004	56.7	33.0	14.1	(7.2)	16.8
2005	37.8	7.3	19.0	13.6	(2.1)
2006	103.8	36.0	37.1	12.5	18.2
2007*	142.2	33.4	61.8	26.3	20.7
2008*	(75.0)	8.3	(48.3)	(20.4)	(14.6)
2009*#	107.7	10.6	71.9	58.7	(33.5)
2010*#	79.4	5.9	74.5	(12.1)	11.1
2011*#	27.1	22.1	(41.4)	21.6	24.8
2012*#	111.6	30.3	42.4	(5.6)	44.5
2013*#	81.2	30.7	54.7	(23.3)	19.1
2014*#	44.7	6.1	(17.8)	43.3	13.1
2015*#	(15.8)	21.0	(63.8)	18.7	8.3
2016*#	68.1	(23.3)	47.1	18.9	25.4
2017*#	264.0	66.0	61.8	71.3	64.9
2018*#	10.9	(33.6)	9.5	-	35.0
2019*#	262.2	60.3	23.5	45.0	133.4
2020*#	235.8	145.0	81.2	121.6	(112.0)
2021* (unaudited)	N/A	N/A	N/A	N/A	11.6

* Excluding valuation changes of the Strategic Portfolio.

Including valuation changes of private equity and real estate investments held under the LTGP.



HONG KONG MORTGAGE CORPORATION



SME FINANCING GUARANTEE SCHEME

- Special 100% Loan Guarantee:
 - Application period extended to 31 December 2021 with enhancement measures introduced:
 - i. Maximum loan amount per enterprise increased from the total amount of employee wages and rents for 12 months to that for 18 months, with an upper limit of HK\$6 million (originally HK\$5 million)
 - ii. Maximum repayment period extended from 5 years to 8 years
 - iii. Principal moratorium period extended from 12 months to 18 months
 - The enhancement measures took effect from 29 March
 - As of 15 April 2021, over 30,300 applications were approved, amounting to about HK\$49.2 billion. Around 19,100 applications have chosen the principal moratorium option



SME FINANCING GUARANTEE SCHEME

- 80% and 90% Guarantee Products:
 - In 2021, as of 15 April, over 1,200 applications were approved, with total loan amount of about HK\$4.1 billion
 - Application period for principal moratorium is extended to 31 December 2021



PERSONAL LOAN GUARANTEE SCHEME

- The Financial Secretary proposed in the 2021-22 Budget to introduce the 100% Personal Loan Guarantee Scheme for unemployed persons:
 - Eligible borrowers should be Hong Kong permanent residents aged 18 or above, who have been unemployed for at least two months at the time of loan application and can demonstrate cessation of main recurrent incomes from employment in Hong Kong
 - Maximum loan amount is six times the average monthly income for any three months within specified period, with an upper limit of HK\$80,000
 - Maximum repayment period is six years, with an option of principal moratorium for the first 12 months
 - Effective fixed interest rate is 1% p.a.; interests will be refunded after the loans are fully repaid by the end of the repayment period
 - Application period lasts for six months from the launch of the scheme



MORTGAGE INSURANCE PROGRAMME (MIP)

- In 2021, as of 15 April, around 17,000 applications have been approved year-to-date, of which over 12,800 are under the new coverage after the MIP revisions in October 2019. Over 90% of approved applications are from first-time homebuyers
- Principal moratorium or extension of repayment schedules is available to borrowers to help reduce their repayment burden



FIXED-RATE MORTGAGE PILOT SCHEME

- Application period has been extended to 30 October 2021
- Fixed mortgage rates for 10, 15 and 20 years are 1.99%, 2.09% and 2.19% per annum respectively
- As the borrowers will be insulated from interest rate movement under the fixed-rate period which is 10 years or longer, stress testing against interest rate rise is not required, but the current debt-to-income ratio requirement is still applicable
- Since the launch of the Pilot Scheme, applications with loan amount totalling almost HK\$270 million have been received



REVERSE MORTGAGE PROGRAMME

- As of 15 April 2021, 4,608 applications had been received:
 - Average age of borrowers: 68 years old
 - Average monthly payout: HK\$16,300
 - Payment terms: 10-year (23.5%);
15-year (15.1%); 20-year (12.5%); life (48.9%)
 - Average property value: HK\$5.6 million
 - Average property age: 30 years



HKMC ANNUITY PLAN

- Premium receipts of around HK\$888 million were recorded in the first three months of 2021, a rapid growth over the same period in 2020
- The average premium amount also rose by 12% to HK\$0.99 million
- Detailed business results:

	2020 FY	2020 (1 st 3 months)	2021 (1 st 3 months)
No. of policies issued	2,606	363	895
Total premium amount (HK\$ million)	2,538	320	888
Average premium amount (HK\$ million)	0.97	0.88	0.99