

## **The Status of Hong Kong as an International Financial Centre**

Many cities in many jurisdictions aspire to be an international financial centre. In the many policy statements by the relevant authorities articulating this aspiration, I notice little reference to what exactly they meant by an international financial centre and what roles they contemplate to perform. Perhaps these issues are so basic that they are taken for granted. I disagree. All public policies must have clear objectives that the public can readily understand and be made on the basis of a sound theoretical foundation. In the absence of these, very simply the public interest may not be well served, in that valuable efforts and resources may be wasted, and public support may be less forthcoming than would otherwise be the case.

In other Viewpoint articles, I have defined “finance” as the mobilization of money from those who have it to those in need of it, and argued that if such mobilization is effectively organized the economy will be well served. A “financial centre” is obviously a place where such mobilization is organized. And an “international financial centre” is where the mobilization money is conducted on an international dimension, involving money of foreign entities (institutions and individuals), whether they are investing it or raising it. Thus, a company from the Mainland raising money in Hong Kong through the issue of shares traded in the stock market of Hong Kong, attracting money from investors from all over the world, is a typical example of such activity. And if this and other types of activities mobilizing money from those who have it to those in need of it on an international dimension are conducted on a large scale here in Hong Kong, then obviously we qualify to be called an international financial centre.

I used the volume of Initial Public Offerings (IPO) of stocks, rather than trading activity measured in terms of the daily turnover in our stock market, for illustration deliberately. The stock market is (merely) a secondary market that provides liquidity and facilitates accurate price discovery of the stocks listed. Indeed, these are the two conditions that enhance the attractiveness of the stock market as a channel for

mobilizing money through IPO activities. But no more than that; even though there are many interests involved in the daily trading activities, including those of stock brokers, traders and the much larger population of investors holding stocks. This is why, in that context, it is called a secondary market and not a primary market; it is only of secondary importance compared with the primary IPO market, which is where money is mobilized to serve the economy. With the volume of IPO offerings in Hong Kong amongst the largest in the world, sometimes surpassing New York and London to be the largest, without doubt we are an international financial centre.

In my opinion, Hong Kong can even claim to be the most international of financial centres in the world, in that the two “legs” in the mobilization of money – investors and fund raisers – are predominantly foreign, for example, fund raisers from the Mainland tapping money from Europe and America. By comparison, if we take New York as an example: yes there is a huge volume of money being mobilized there, but if one looks at the matter carefully, one finds that either one of the two legs is predominantly domestic, in that foreign companies list their shares in New York to attract money from US investors and foreign investors go to New York to invest in financial assets issued by US entities. New York is important as an international finance centre because its home economy – the US – is the largest in the world, with huge amounts of US money wishing to invest overseas and a large number of US entities wishing to raise money from overseas. For Hong Kong, we are merely a city of seven million people and a small economy, and yet we are playing such an important role in international finance. But obviously we should not be complacent and, in any case, rankings of this nature are never quite meaningful enough to brag about. I mention it to sharpen our focus on what are the roles of an international financial centre.

It is particularly important for Hong Kong to be focused. Article 109 of the Basic Law says that: “The Government of the Special Administrative Region shall provide an appropriate economic and legal environment for the maintenance of the status of Hong Kong as an international financial centre”. I am sure that this is a

heavy responsibility that the HKSARG takes seriously. Indeed, it does; and the results speak for themselves. But international finance is in a state of flux. Many economies are still nursing from the wounds inflicted by the 2007-08 crisis. The developed markets are still talking about the normalization of monetary policy. The process of shrinking the balance sheet of the central bank and the withdrawal of the huge volume of liquidity injected through quantitative easing are only starting in the US; in Europe these are just talks for the time being; in Japan talks have not even started. Less liquidity and higher interest rates will have implications for the prices of financial assets that have been pushed to record levels by the excessive liquidity injected through quantitative easing. Meanwhile, investment banks, particularly those in Wall Street, are getting excited about the prospects of de-regulation and renewed market volatility induced by the normalization of monetary policy! There is also widespread geo-political tension that may well erupt into something ugly and destabilizing to international finance. It is a scenario that we have not experienced before. As an international financial centre, we need, more so than before, to be vigilant and focused.

In the work to maintain the status of Hong Kong as an international finance centre in accordance with Article 109 of the Basic Law, there is one strategic focus that we should always bear in mind and direct our efforts accordingly. Accepting my definition of an international financial centre, we should realistically be concentrating in the mobilization of money between the Mainland and the rest of the world, whether it is the mobilization of money from the rest of the world into the hands of Mainland fund raisers or the mobilization Mainland money into the hands of fund raisers in the rest of the world. Investors in the rest of the world are attracted by what Hong Kong can offer when they wish to invest in financial instruments issued by Mainland entities. They would not come to Hong Kong to look for financial assets issued, for example, by fund raisers in the US or Europe. Equally, the many entities around the world wanting to raise money would not come to Hong Kong unless they are interested in money originating from the Mainland (policy permitting). Our strategic focus should, therefore, be the mobilization of money between the two geographical

or jurisdictional “legs”, namely, the Mainland and the rest of the world.

I can almost hear the criticism of some that Hong Kong, including our financial system, is quickly becoming “Mainlandized”, as if it is something evil. I must say frankly that, insofar as the financial system of Hong Kong is concerned, there is no meaningful international role to play if it is not because of the need to mobilize money between the Mainland and the rest of the world. This is an area of activity that we all should, in fact, welcome and be thankful instead. The financial activities supporting a small economy with seven million people simply do not justify a financial system of our size and do not make us an international financial centre. Our highly international financial system is itself a substantial part of the Hong Kong economy providing a lot of jobs and attractive incomes, supporting much domestic consumption and the livelihood of those employed in other sectors of the economy.

We have made considerable progress in the mobilization of money between the two “legs”. There are, of course, the now familiar Shanghai-Hong Kong Connect and Shenzhen-Hong Kong Connect for stock trading, which have I am sure raised the general interest of investors in the rest of the world in Mainland stocks and Mainland investors in stocks listed in Hong Kong. Hopefully, these will in time, and with the necessary (Mainland related) policy adjustments, lead to more entities in the two “legs” to organize listings in Hong Kong. There is also the Bond Connect which opens up the bond channel for the mobilization of money between the Mainland and the rest of the world through Hong Kong, particularly if in time two-ways flows are allowed. There are many other opportunities, as long as we stay focused in the role in the mobilization of money between the Mainland and the rest of the world. The current efforts in structuring a platform in Hong Kong for the mobilization of money from the Mainland and other economies to fund infrastructural projects along “One Belt, One Road” are right on. I wish them well, although I would not underestimate the difficulty in dealing with the politics of the project, given the many interests of the many jurisdictions involved. The hope is, of course, that the Mainland’s leadership and influence in all this, and its recognition of the role that Hong Kong can play (and

play distinctly well), would help.

With capital controls still being implemented on the Mainland, such mobilization of money between the Mainland and the rest of the world will obviously involve specific policy decisions concerning the capital account by the financial authorities on the Mainland, specifically the People's Bank of China. Outside of the Mainland, Hong Kong knows the capital account of the Mainland of China and the relevant policies best, and is also in the best position to offer advice on how international capital flows can be mobilized in the best interest of China. We are also in the best position to assist in the actual mobilization, through providing a safe and efficient financial platform that addresses both risks and opportunities. We need to remind the financial authorities on the Mainland of the utility of Hong Kong as the international financial centre of China and that using the financial services of Hong Kong is in the national interest. For the effective maintenance of monetary and financial stability, against the background of a rather confused state in international finance, the Mainland still needs some form of capital controls and for some time to come. My hope is that this will give us enough time to achieve such a critical mass as the international financial centre of China as to be indispensable, even if capital account openness is eventually achieved on the Mainland. But I don't know much time we have. So let us stay focused.

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