Chief Executive's Statement

What a turbulent year of 2009! The world experienced the most serious financial crisis since at least the Second World War and, although the worst effects of the crisis lessened during the year, there was a high degree of concern at how the world economy and financial system were coping, and what the effects on Hong Kong would be.

It was therefore not hard to identify my priorities when I took over as Chief Executive of the HKMA on 1 October, and I announced them to the community on my first day.

First, maintaining monetary stability in Hong Kong through the Linked Exchange Rate system. The latest crisis has demonstrated, once again, the value of the Link in ensuring monetary stability, which is of such importance to an open and highly externally oriented economy like ours. In its 26-year history, the link to the US dollar has provided an anchor for the economy through a number of crises. It continues to be the best guarantee of financial stability. 2009 saw unprecedentedly large inflows of funds into the Hong Kong dollar – around HK$640 billion between the last quarter of 2008 and the end of 2009 – as investors viewed Asia, and especially China, as the area that would recover first and most strongly from the global recession. As a result, Hong Kong's Monetary Base exceeded one trillion dollars at the end of the year, and the HKMA issued an additional $374.4 billion in Exchange Fund Bills during the year to meet demand from authorized institutions for liquidity management. The markets reacted calmly to the exit in March from the temporary liquidity-assistance measures introduced in September 2008.

Secondly, maintaining the stability of the banking system and the smooth functioning of credit markets. The Hong Kong banking system has come through the latest crisis in much better shape than many of its counterparts in the US and Europe. The aggregate capital adequacy ratio of the banking sector at the end of 2009 stood at 16.9% and the liquidity ratio at 47.8%. The classified loan ratio, despite an increase from 2008, remained low at 1.35% and other asset-quality indicators continued to be favourable.

Following the liquidity measures taken in 2008, the Hong Kong interbank market largely returned to normal functioning in 2009 with interbank interest rates declining to very low levels in line with their US-dollar counterparts. Confidence in the local banking system was greatly strengthened while access to bank finance by corporates, including the small and medium-sized enterprises, has largely been restored with the help of the Government loan guarantee schemes. However, we need to guard against the risk of a credit fuelled asset bubble in Hong Kong that would threaten banking and financial stability. This was why the HKMA tightened the loan-to-value ratio for the top end of the property market (those valued at $20 million or more) to 60% in late October.

Another major task for the HKMA in 2009 was continuing to deal with the over 21,000 complaints from bank customers in relation to the sale by banks of investment products related to the failed US investment bank Lehman Brothers. In July the HKMA and the Securities and Futures Commission, following extensive investigations by both regulators, reached a settlement agreement with 16 banks with regard to the sale of the Lehman Minibonds. The agreement allowed the vast majority of the banks' affected customers to get back at least 60% of their principal and those aged 65 or above to receive 70%. By the end of the year, the HKMA had finished its investigation work on 77% of the Lehman-related complaint cases. Our aim is to complete the investigation of the bulk of those remaining by the end of March 2010.

Thirdly, continuing with the prudent investment of the Exchange Fund. The global financial markets continued its nose dive in the first quarter, resulting in substantial losses of the Exchange Fund. However, the sharp rebound in global equity markets from the second quarter helped the Fund to achieve eventually an investment return of $106.9 billion or 5.9% in 2009, more than recouping the $75 billion investment loss in 2008. Given the considerable uncertainties surrounding the global financial markets, the HKMA will continue to manage the Exchange Fund prudently in accordance with the investment objectives determined by the Financial Secretary on the advice of the Exchange Fund Advisory Committee.

Finally, developing Hong Kong further as an international financial centre. With the increasing size of the Mainland economy and its influence in the global economy, our ability to intermediate renminbi fund flows is essential for Hong Kong's future competitiveness as the leading international financial centre in the region. A major breakthrough was achieved in July 2009, with the introduction of the pilot scheme for settlement of cross-border trades in renminbi, followed by the issuance of several renminbi bonds in Hong Kong. The Ministry of Finance of China issued in Hong Kong the first sovereign bond outside the Mainland.

Of course, a great deal of other work was undertaken by the HKMA during a very busy and challenging year, and the details are set out in the following chapters. I should add that much of the achievements of the HKMA in 2009, and for that matter in the years before, would not have been possible without the very solid foundation laid by my predecessor, Mr Joseph Yam, who had been at the helm for 16 years since the HKMA was set up in 1993. Under Joseph's capable leadership, the HKMA has gained respect and recognition locally and internationally as a highly professional central banking institution with an outstanding track record in coping with successive crises over the years. I am sure that my colleagues in the HKMA will join me in thanking Joseph for his leadership and contributions to the HKMA.

Looking ahead, we will continue to face numerous challenges. The global economic outlook for 2010 seems far from certain: a recovery appears to be underway but its strength and sustainability remain to be seen. The fiscal positions of the major economies and the timing and pace of their exits from monetary easing make the way ahead difficult to discern. Uncertainty about the direction and size of movements in interest rates and fund flows are likely to mean that financial markets will remain volatile. The HKMA will exercise great caution and vigilance both as regulator of the banking system and manager of the Exchange Fund. As Chief Executive, I am acutely aware of the need not just to discharge our duties effectively but also to be able to explain clearly to the community what we do and to gain their trust and support!

Norman T.L. CHAN
Chief Executive