



Chief Executive's Statement

The year of 2019 has been anything but uneventful.

US-China trade tensions remained a big wild card. Lingering uncertainties over trade talks between the world's two largest economies rattled investor confidence and undermined international trade, manufacturing, investment and even consumption. Gone are the days when global economic expansion was a given. The global economy entered a synchronised slowdown during the year. In response to the slower growth, major central banks around the world have reversed course on their monetary policy normalisation.

Locally, social incidents happening in the second half of the year dealt a further blow to the Hong Kong economy. The retail, tourism and catering sectors were among the hardest hit. For 2019 as a whole, the Hong Kong economy contracted by 1.2%, the first annual decline in a decade, while the unemployment rate rose to 3.3% from a multi-year low of 2.8% at the beginning of the year. As 2020 dawned, the novel coronavirus (COVID-19) outbreak posed yet another significant threat to both global and local economies.

In the face of such an uncertain and challenging environment, it is of paramount importance to maintain monetary and financial stability in Hong Kong, as I made clear when taking over as Chief Executive of the HKMA on 1 October 2019.

Monetary and financial stability: the bedrock of an international financial centre

The Linked Exchange Rate System (LERS) in place since 1983 has helped Hong Kong weather numerous challenges and shocks, demonstrating its important role as an anchor of Hong Kong's economic prosperity and status as an international financial centre. Notwithstanding the challenging external and domestic environment during the year, the LERS continued to operate in a smooth and orderly manner, once again proving its resilience in times of uncertainty. Hong Kong's banking system also remained sound and robust. The facts speak for themselves: the Hong Kong dollar exchange rate remained stable and has strengthened to the strong side of the Convertibility Zone in recent months, while bank deposits continued to grow during the year. In a nutshell, no noticeable outflow of funds from the Hong Kong dollar or the banking system was observed.

The stability of Hong Kong's monetary and banking systems reflects not only the robustness of, but also strong confidence in, our systems. This did not happen overnight, but through years of efforts to build up buffers and strengthen surveillance, complemented by our swift response to rumours on social media platforms.

Chief Executive's Statement

Our preparations over the years for rainy days have built a solid foundation and strong buffers for Hong Kong's monetary and banking systems. In addition to the vast foreign exchange reserves in our public coffers, our banking system has strong capital buffers, robust liquidity and very good asset quality, whether by international or historical standards. The eight rounds of countercyclical macroprudential measures on property mortgages implemented since 2009 have also greatly enhanced banks' resilience against a property market downturn.

Market surveillance and banking supervision make up the core part of our work in maintaining monetary and banking stability, and we have been strengthening our surveillance and supervisory framework from time to time. Apart from close monitoring of the credit and liquidity risks of banks, one of our new endeavours in the year was to make use of technology and granular data collected from banks to enhance our capability to monitor Hong Kong dollar funding and financial market activities in a more in-depth and timely manner. Stress tests and contingency planning have also been augmented in the light of the fast evolving economic and operating environment.

Indeed, our robust regulatory regime has won strong endorsements internationally. During the year, the International Monetary Fund reaffirmed that Hong Kong was well placed to address both cyclical and structural changes, given its significant buffers. Hong Kong's effective legal and institutional framework for combatting money laundering and terrorist financing also obtained a positive assessment from the Financial Action Task Force (FATF), making Hong Kong the first in the Asia-Pacific region to achieve an overall compliant result in the FATF's Mutual Evaluation.

Confidence is the foundation for the proper functioning of markets and is crucial to the safeguarding of monetary and financial stability. To maintain market confidence, we have to be on high alert for, and respond swiftly to, any malicious rumours that may potentially cast doubt on Hong Kong's monetary or banking systems. This is particularly important

given the prevalent use of social media and instant messaging nowadays. While a variety of rumours were spread on social media platforms by fearmongers during the outbreak of social unrest, our quick and clear rebuttals to these rumours through social media, in addition to traditional media, proved useful and effective in clearing the air, quelling false rumours from spreading further, and upholding international and public confidence in our systems.

Banking system: an important pillar of economic activity

The banking sector, as an essential pillar of economic activity, plays a fundamental role in ensuring the smooth running of society and the economy. Despite the challenging operating environment since the latter half of the year, banks have been working hard alongside others and doing their utmost to maintain normal operation of their core functions and continue serving businesses and the public.

In addition to basic banking services like deposits and transfers, an important function of banks is in extending credit to borrowers in support of the real economy. We are well aware of, and concerned about, the cash-flow problem facing businesses, especially small and medium-sized enterprises (SMEs), under the difficult economic conditions. While safeguarding banking stability, we have launched a number of initiatives to ensure continued funding support to SMEs. In particular, the Countercyclical Capital Buffer ratio of banks was reduced on two occasions, in October 2019 and March 2020, by a total of 150 basis points to 1.0%; the level of regulatory reserve requirement on banks was also reduced by half in April 2020. These measures release a total of around HK\$1 trillion in lending capacity, providing banks with more room for lending to enterprises including SMEs. We have also set up a platform – the Banking Sector SME Lending Coordination Mechanism – bringing together major banks in Hong Kong to explore and discuss specific measures to strengthen funding support for SMEs. I am pleased to see that many banks have responded proactively to our call and introduced relief measures such as principal moratorium for customers in need to ride out the storm.

Chief Executive's Statement

In view of some SMEs' feedback about difficulties in opening bank accounts, which is the very first step in accessing various banking services, we have made dedicated efforts to address this issue over the past few years. Our work is bearing fruit, as improvement in account opening for businesses is visible. As a further step to promote financial inclusion, the HKMA spearheaded the launch of tiered account services – Simple Bank Accounts (SBAs) with a streamlined customer due diligence process – to provide start-ups and SMEs with an alternative to traditional bank accounts. More than 2,800 SBAs have been opened so far.

International financial centre: from strength to strength

We have always been mindful of the need to strike a reasonable balance between regulation and development. Given the intense competition among financial centres, we have to work hard to strengthen Hong Kong's competitiveness as an international financial centre and thereby ensure its longer term stability. There are four key areas of work: technology, green finance, financial connectivity with the Mainland, and talent development.

Embracing technology in the digital era

Hong Kong has been moving fast in promoting financial technology (fintech) since the establishment of the HKMA Fintech Facilitation Office in 2016 and the introduction of the Smart Banking initiatives in 2017.

On the payment front, the vibrancy of the fintech ecosystem is evident in the strong momentum in the adoption of the Faster Payment System (FPS), the world's first multi-currency, cross-banks and e-wallets, real-time retail payment platform. FPS registrations reached four million within a short span of 15 months, representing a high rate of penetration in a population of 7.5 million people. The Government has also adopted the FPS to provide the public with greater convenience in paying taxes, rates and water charges. More and more businesses are expected to use this fast, safe and convenient means of receiving and making payment to enhance operational efficiency.

In the banking sector, significant progress was seen in applying fintech to their banking services and business operations. According to a study conducted by the HKMA, almost 90% of the surveyed retail banks have adopted, or are planning to adopt, artificial intelligence in their business applications. With the HKMA's facilitation, banks have been applying big data and consumer behavioural analytics in their personal credit products. They have also launched over 800 Open Application Programming Interfaces in the first two phases, covering a range of banking products and services. While encouraging banks to use fintech, we did not lose sight of the need for enhanced technology risk management and consumer protection in digital banking services. Timely supervisory guidance has been provided to banks in these areas.

Regulatory technology (Regtech) is another area of great interest to banks, for its potential of enabling banks to conduct regulatory compliance and risk management, particularly in anti-money laundering and counter-financing of terrorism (AML/CFT), more efficiently and cost-effectively. To facilitate greater industry adoption of Regtech and the building of a wider Regtech ecosystem, the HKMA organised the inaugural AML/CFT Regtech Forum and issued its first Regtech newsletter in November to discuss possible use cases of Regtech. At the same time, the HKMA, as a banking supervisor, is exploring the use of supervisory technology (Suptech), including new data science and analytics, to enhance work effectiveness and efficiency. We have embarked on a series of studies and developed a road map for the implementation of Suptech in the next few years.

From a broader perspective, this is only the start of the fintech journey in the banking sector. The HKMA granted eight licences to virtual banks during the year. One of the virtual banks officially launched its services in March 2020, while some other virtual banks have commenced pilot trials through the HKMA's Fintech Supervisory Sandbox. I look forward to the launch of the other virtual banks and the introduction of more innovative and diversified banking services to the people of Hong Kong that would help raise the global competitiveness of our banking sector.

Chief Executive's Statement

More exciting developments are also expected at the international level. After successfully completing a Proof-of-Concept (PoC) trial to connect our blockchain-based trade finance platform, eTradeConnect, with its European counterpart, we are conducting another PoC trial with the platform of the People's Bank of China, paving the way for the digitalisation of cross-border trades. We have begun a joint research project with the Bank of Thailand to study the application of Central Bank Digital Currency to cross-border payments. The Bank for International Settlements also put its first Innovation Hub Centre into operation in Hong Kong in November to foster fintech collaboration within the central banking community. All these developments present clear evidence of Hong Kong's leading global position in fintech development.

Promoting green and sustainable finance for a better future

Climate-related risks have drawn increasing global attention in recent years. To contribute to the global efforts in addressing this challenge, the HKMA unveiled three key measures in May to promote green finance development in Hong Kong in different capacities.

As a banking supervisor, the HKMA is undertaking a three-phased approach to promoting green and sustainable banking. A framework for assessing the "greenness" of banks has been developed for industry consultation under Phase I, paving the way for the formulation of supervisory expectations and requirements for the banking industry under Phase II and implementation under Phase III.

As the manager of the Exchange Fund, the HKMA actively advances responsible investment by integrating environmental, social and governance (ESG) factors into its investment activities. Specifically, we have adopted the principle of giving priority to green and ESG investments if their long-term return is comparable to other investments on a risk-adjusted basis. After venturing into the green bond market in 2015 as one of the early investors, we will continue to grow our green bond portfolio and invest in other ESG assets. We will also join hands with like-minded investors and regulators to promote best practices on ESG through our participation in international organisations in the ESG community.

Other than addressing climate-related risks, green finance offers enormous opportunities for Hong Kong's financial markets, particularly in bond and project finance markets. As a market facilitator, the HKMA plays an active role in promoting Hong Kong as a major global hub for green finance. In May, we assisted the Government in issuing an award-winning green bond under the Government Green Bond Programme, setting an important new benchmark for potential green bond issuers in Hong Kong and the region. We have also established the Centre for Green Finance under the HKMA Infrastructure Financing Facilitation Office with the mission of promoting capacity building and experience sharing in green finance.

Over and above all these actions, we are conscious of our vital role in supporting and enabling the sustainable development of society as a whole. I am pleased to present a new dedicated chapter on corporate social responsibility in this year's *Annual Report*, setting out our strategy and major initiatives in promoting a sustainable and environment-friendly marketplace, supporting the wider community, protecting the environment, and nurturing a caring workplace.

Consolidating our unique role as dominant gateway to Mainland China

Since 2014, a number of unique cross-border investment channels have been established, including Mutual Recognition of Funds, Stock Connect and Bond Connect. Over the years, both Bond Connect and Stock Connect have been enhanced, providing more convenience and flexibility for international investors to invest in onshore securities on the Mainland. Currently, the two Connect schemes handle over 60% of the onshore trading of Mainland bonds and stocks, respectively, by international investors, underscoring Hong Kong's unique value as the conduit between Mainland China and the rest of the world. Through Hong Kong's platform, international investors can get the best of both worlds: grasping opportunities in Mainland China while continuing to use the legal and regulatory framework, market practices and languages to which they are accustomed.

Chief Executive's Statement

During the year, a major policy breakthrough was secured in establishing Wealth Management Connect, which will mark yet another milestone in mutual financial market access between Hong Kong and the Mainland and reinforce Hong Kong's position as the leading global hub for offshore renminbi business. We are working closely with the Mainland authorities to formulate the implementation details with a view to launching it as soon as possible.

At the same time, good progress has been achieved in rolling out financial facilitation measures to support the development of the Guangdong-Hong Kong-Macau Greater Bay Area. The usage of Hong Kong e-wallets in the Mainland has expanded to cover some 800,000 merchants. Hong Kong residents are also allowed to open personal Mainland bank accounts remotely. We will seize every opportunity to gain more policy headroom for the introduction of further financial facilitation measures, particularly for corporates and financial institutions, as well as the enhancement of existing measures.

Upgrading soft power to enhance long-term competitiveness

Talent is crucial to the sustainable and sound development of an international financial centre. After months of preparation, the Hong Kong Academy of Finance (AoF) was established in June with the mission of promoting financial leadership and monetary and financial research. Over 160 senior executives from financial institutions, professional firms, academia and regulatory bodies are now AoF members. The AoF has held a number of talks under its leadership development programme and initiated four applied research projects within the first six months of operation.

Fintech is a major focus of talent development. The Fintech Career Accelerator Scheme 2.0, which includes providing internship opportunities as well as regulatory and technology training to students in collaboration with strategic partners, benefitted over 220 students during the year. We also launched the Fin+Tech Collaboration Platform jointly with the Hong Kong Science and Technology Parks in November. It will provide a useful platform for organising fintech-related activities such as accelerators and hackathons to explore innovative solutions, identify talent and seek collaboration opportunities.

The HKMA itself is also introducing new technologies and applying new data science and analytics. We will be upgrading our skill sets and capabilities alongside the industry.

Exchange Fund: safeguarding the wealth of Hong Kong people

Benefitting from the strong performance of the global stock and bond markets, the Exchange Fund achieved the second highest investment income on record of HK\$262.2 billion during the year, representing an investment return of 6.6%. In particular, the Long-Term Growth Portfolio posted a decent annualised internal rate of return of 12.6% since inception. Such achievements are not easy, having regard to the need to preserve good credit quality, liquidity and defensiveness for the Exchange Fund to enhance its resilience to market shocks and to fulfil its statutory purposes.

In March 2020, global stock markets experienced extreme volatilities and wild roller-coaster rides, with US and European stock indices suffering the worst fall since the 1987 market crash on growing fears over the spread of COVID-19. In the face of the ever-changing global financial landscape, we will continue to manage the Exchange Fund in a prudent and agile manner, and adhere to the established principle of "Capital Preservation First, Long-Term Growth Next" to safeguard and grow the wealth of Hong Kong people.

Chief Executive's Statement

Serving the public interest with professionalism and dedication

These are extraordinary times for Hong Kong. Every one of us must stay calm and vigilant. I have every confidence that together, we can ride out the present challenges, as we have done in numerous crises over the past decades. Our buffers are strong. Our fundamentals are intact. Our strengths are well-entrenched. The HKMA's capability, resources and determination to maintain Hong Kong's monetary and financial stability are beyond doubt.

This is my first statement after assuming office as the Chief Executive of the HKMA. While the path ahead may be filled with challenges, it has always been my firm belief that every challenge we face is also an opportunity. My colleagues and I, as a team, will continue to serve the people of Hong Kong with professionalism and dedication, and put our best foot forward to maintain monetary and financial stability while strengthening Hong Kong's status as an international financial centre.



Eddie Yue

Chief Executive