Chief Executive's Statement

Resilience in the face of adversity

Reverberations from slowing global economic growth amid a "high for longer" interest rate environment and intensifying geopolitical tensions — not just stemming from the Russia-Ukraine war and China-US tensions but also the outbreak of conflict in the Middle East — were the key themes for the financial markets in 2023. The March banking turmoil in the US and Europe, the most significant system-wide banking stress since the 2008 Global Financial Crisis, weighed further on market sentiment. Major economies grappled with the harsh realities of tightened monetary conditions and greater uncertainty over the inflationary path and interest rate outlook. Adding to the uncertainty was the pace of Mainland China's economic recovery, which was slower than general market expectations.

With volatility and unpredictability becoming the "new normal" in financial markets, Hong Kong has again demonstrated its well-known ability to adapt, showing remarkable resilience. Since the city's full-fledged post-COVID reopening last year, much work has been done to attract people back to our dynamic city and reconnect them with Hong Kong. The HKMA has contributed by hosting a series of large-scale international events such as the Global Financial Leaders' Investment Summit and conferences with the Bank for International Settlements (BIS), which showcased our vibrant city and helped send the message worldwide that Hong Kong, as a major international financial centre (IFC), is open for business and remains the centre of action and innovation. There are clear signs of gradual recovery, driven by an encouraging revival of inbound tourism and improved private consumption, also supported by a resilient labour market and the various support measures rolled out by the Government. For 2023 as a whole, Hong Kong's gross domestic product growth bounced back to 3.2% from negative territory in 2022.

The HKMA entered its fourth decade in 2023. The past 30 years have seen the dynamics of the economy and the financial markets change drastically, with technology driving advances beyond anyone's wildest imagination. The invaluable experience and wisdom gained over the past three decades have enabled us to face the future with confidence. Despite macroeconomic headwinds and an uncertain external environment, the HKMA will continue to uphold its mandate of safeguarding monetary and banking stability in Hong Kong, and will actively pursue developmental opportunities to anchor that stability and cement the city's status as a leading IFC.

Chief Executive's Statement

Former and current Financial Secretaries of the Government of the Hong Kong Special Administrative Region and Chief Executives of HKMA at a gathering to celebrate the HKMA's 30th anniversary: (from left) Mr Joseph Yam, Mr Henry Tang, Mr Donald Tsang, Mr Paul Chan, Mr Eddie Yue, Mr Antony Leung, Mr John Tsang, and Mr Norman Chan

LERS – Weathering the storms

Last year marked the 40th anniversary of the Linked Exchange Rate System (LERS), a staunch pillar supporting Hong Kong's strong and stable monetary and financial systems. Four decades of transparent and effective operation have nurtured confidence in the LERS and its credibility in the market. Throughout the year, the Hong Kong dollar stayed within the Convertibility Zone and the Hong Kong dollar market operated smoothly, reflecting the strong market confidence in the LERS, a confidence also shared and expressed by the International Monetary Fund and global market players.

Behind this confidence lie the HKMA's proactive efforts in public and market engagements, along with effective surveillance. We spared no effort during the year in communicating with key stakeholders to foster a clear understanding of the functioning of the LERS, which is all the more important in times of volatility, be it stemming from economic stress or political uncertainties. We also strengthened surveillance of our monetary system, leveraging the use of datasets from the trade repository and expanded granular data from banks, as well as advanced data analytics and artificial intelligence, to enhance our capability, enabling more timely and comprehensive analysis of financial stability and macro-prudential surveillance.

Banking system – A major source of stability

Despite a multitude of challenges including the high-interest-rate environment, persistent geopolitical tensions and a challenging credit landscape, Hong Kong's banking system remained stable throughout the year, underpinned by strong capital and liquidity buffers.

As at the end of 2023, the consolidated total capital ratio of local banks stood at 21.1%, well above the international minimum requirement of 8%. The Liquidity Coverage Ratio of large banks edged up to 178.6% as of the fourth quarter of 2023, likewise well above the statutory minimum requirement of 100%. While the classified loan ratio increased slightly from 1.40% at the end of 2022 to 1.56% at the end of 2023, it remained below the long-term historical average of 2.0%. The increase was mainly driven by exposures to Mainland privately-owned enterprise (POE) property developers; but such exposure levels were generally well-contained as a result of banks' prudent credit risk management over the years, and the overall asset quality of the banking sector remained sound.

Chief Executive's Statement

What caught most market players by surprise in 2023 was unquestionably the banking turmoil in the US spilling over to Europe, which created a level of system-wide banking stress unseen since the 2008 Global Financial Crisis. The HKMA remained on high alert as the situation unfolded and took a number of precautionary actions to limit any potential adverse spillover effects on confidence in the local banking and financial systems. This, coupled with the strong capital and liquidity buffers maintained by banks in Hong Kong, meant that our banking sector was largely unaffected by the turmoil, remaining resilient even as the global financial markets were roiled. In the aftermath of this episode, the HKMA conducted a comprehensive internal review with a view to drawing out lessons for the local banking sector and strengthening the HKMA's supervisory effectiveness and agility to handle a banking crisis should one occur.

While prudent credit risk management is important, we have always reiterated our supervisory expectation for banks to be mindful of the need to support the real economy. As the orderly exit from the banking sector's Pre-approved Principal Payment Holiday Scheme commenced in July 2023 with the economic effects of COVID-19 receding, the HKMA worked closely with banks to ensure a gradual and smooth transition to normal loan repayment with flexibility for those borrowers who continued to be under pressure. Earlier this year, recognising that some small and medium-sized enterprises are still facing challenges in their operations despite the end of the pandemic, nine new measures were rolled out to further assist them in obtaining financing from banks.

Having reviewed the risks associated with the local property market in the context of banks' property lending, the HKMA announced in July 2023 the first relaxation of the countercyclical macroprudential measures for residential properties since their introduction in 2009. This relaxation increased the loan-to-value ratio cap for most residential mortgage loans as well as for financing for property development and investment. It was later followed by suspension of the interest rate stress testing requirement in early 2024.

The HKMA's supervision of financial institutions has been moving with the times. With recent years having seen a sharp global increase in fraud cases, we have considerably stepped up our efforts to counter new fraud tactics by introducing a holistic set of measures to protect bank customers. These include enhancing information sharing between banks and with law enforcement agencies; strengthening the monitoring of suspicious transactions (including implementation of real-time fraud monitoring and tightened payment card authentication); empowering customers to have more controls on their payment cards; and educating customers and raising public awareness of frauds with the launch of the Anti-Scam Consumer Protection Charter, as well as a pre-transaction alert mechanism which warns users if a higher-risk Faster Payment System (FPS) transaction is spotted.

In light of a proliferation of innovative and digital banking products and services, the HKMA has worked with the banking industry to step up consumer and investor protection more broadly and enhance the banks' operational and cyber resilience, as well as their collective defences against systemic cyber events. At the same time, all major banks have considerably strengthened their capabilities to respond to, and recover from, destructive ransomware attacks. The HKMA together with the industry has also pursued various consumer data infrastructure projects, such as the "Credit Data Smart" pilot programme to enhance consumer credit reference services, and taken forward a cross-boundary credit reference initiative to facilitate cross-boundary financing activities by corporates.

Fintech and digitalisation can bring about enormous opportunities when the risk is properly managed. Leveraging earlier success in facilitating the uptake of Regtech, the HKMA, with the support of the Securities and Futures Commission (SFC) and the Insurance Authority, published a new Fintech Promotion Roadmap in August 2023 to promote further development of fintech by financial institutions in five focus areas — Wealthtech, Insurtech, Greentech, artificial intelligence and distributed ledger technology. We anticipate local regulators continuing to collaborate and work closely together with their industry sectors in the coming years in order for the Hong Kong financial industry as a whole to keep abreast and reap the benefits of dynamic fintech development.

Chief Executive's Statement

Hong Kong as an IFC — The centre of action and innovation

In 2023, we fully emerged from the pandemic. Hong Kong was not only back in business but its position as one of the world's leading IFCs was further underscored by the return of global investors and our strengthened global network. Domestically, we took the opportunity of the 30th anniversary of the HKMA's establishment to host a series of large-scale, international events with top-level participation from the global financial and banking community to demonstrate Hong Kong's vibrancy and to send a clear message that Hong Kong as an IFC remained relevant and indispensable to global investors and financial institutions seeking growth and innovation. Of particular note was the return of the Global Financial Leaders' Investment Summit, held in November, which attracted to our city more than 350 international and regional leaders from some 160 global financial institutions. Other high-powered events hosted in Hong Kong included a meeting of the Basel Committee on Banking Supervision (Basel Committee) and two HKMA-BIS Conferences which were among the largest gatherings of central bank governors and banking supervisors of the year. These events attest to the global financial sector's commitment to and confidence in Hong Kong.

Externally, 2023 was also a year in which Hong Kong proactively reached out to strengthen its connections with traditional markets including the US and Europe, as well as new destinations such as those in the Middle East. We met with peer regulators and top management of global financial institutions in these markets to both apprise and update them on the opportunities in Hong Kong and the Mainland, while seeking out new collaboration opportunities for Hong Kong.

To complement these engagement efforts, we actively contributed to the work of international and regional forums by taking up certain leadership roles. During the year, I accepted invitations to chair the BIS Meeting of Governors from Major Emerging Market Economies and to co-chair the Financial Stability Board (FSB)'s Regional Consultative Group for Asia. My colleagues are also chairing or co-chairing a number of other important groupings under the Basel Committee, the Financial Action Task Force, and the Executives' Meeting of East Asia-Pacific Central Banks, to name a few. The HKMA's leadership at many regional and international forums is a recognition of Hong Kong's expertise and contribution to international central banking and regulatory efforts in the pursuit of global monetary and financial stability, as well as Hong Kong's importance as an IFC.

To build on the above accomplishments, we must position ourselves as a forward-looking IFC, staying ahead of the curve to ensure our ongoing competitiveness. We have identified three long-term trends in the coming years that will shape our future: namely the continued opening-up of the Mainland, the development of green and sustainable finance and the deployment of fintech. We will continue to support the development of our financial markets to capture the opportunities from these long-term trends while positioning our financial platform to provide leading services to attract more businesses to Hong Kong. For details of our work on green and sustainable finance, readers may refer to our *Sustainability Report 2023*.

Chief Executive's Statement

Mainland opportunities

We continued in 2023 to leverage our unique advantage by promoting and developing our gateway role to the Mainland market as well as our position as the global hub for offshore renminbi business. Concerted efforts were made to deepen and widen the mutual market access schemes with the Mainland. During the year, a series of enhancements to the Cross-boundary Wealth Management Connect scheme were introduced to expand significantly the scope of investment products covered by the scheme and enhance the sale and promotion processes, further widening mutual access to wealth management markets in the Guangdong-Hong Kong-Macao Greater Bay Area (GBA). To underpin the smooth operation of the Southbound leg of the Bond Connect scheme, nine market makers were added to improve secondary liquidity and meet investor demand. In May 2023, the Northbound Trading leg of the Swap Connect scheme was launched, providing global investors with a convenient and secure channel for trading interest rate swap products in the Mainland to facilitate their management of interest rate risks.

Another notable development was the joint announcement in January 2024 by the HKMA and the People's Bank of China of six new measures to deepen financial co-operation between Hong Kong and the Mainland. They include promoting the use of onshore bonds as eligible collateral in offshore markets, starting with the HKMA's Renminbi Liquidity Facility, and further opening up the onshore repo market. These measures would enable Bond Connect investors to better manage liquidity using their existing onshore bond holdings.

We have also made significant progress in our initiatives to make fund transfers within the GBA more convenient for the general public and for corporates. These include facilitative measures for cross-boundary fund flow management by GBA corporates and remittance for purchasing properties in GBA Mainland cities by Hong Kong residents.

The year 2023 also saw further stellar growth in renminbi business, with broad-based expansion across bank deposits, trade settlement payments, and particularly offshore bond issuances and bank lending. To further reinforce Hong Kong's role as the leading offshore renminbi business hub, we have been working to expand the range of offshore renminbi products. In collaboration with the SFC and Hong Kong Exchanges and Clearing Limited, the HKD-RMB Dual Counter Model and the Dual Counter Market Making Programme were launched. These initiatives will facilitate the use of renminbi in equity trading in Hong Kong and represent a significant step in expanding our renminbi investable universe.

Progress made in these areas presents new opportunities for Hong Kong's financial institutions and reinforces our position as the dominant gateway to the Mainland and the pre-eminent global offshore renminbi hub, as well as our role as a global risk management centre.

Fintech

Embracing fintech is another critical success factor in upholding Hong Kong's position as a leading IFC. A clear roadmap was laid down in 2021 when we unveiled the "Fintech 2025" strategy. Three years on, significant progress has been made on all fronts of this strategic plan. In particular, we reached important milestones in our Central Bank Digital Currency (CBDC) journey. On the wholesale level, the Multiple CBDC Bridge (mBridge) platform, co-founded by the HKMA and a number of central banks under the auspices of the BIS Innovation Hub, is progressing to the Minimum Viable Product (MVP) phase. The aim is to use CBDC to cut the cost and time of cross-border settlements, and we target to launch the MVP in 2024 to pave the way for a full production system. On the retail front, building on the success and experience of Phase 1 of the e-HKD pilot programme last year, Phase 2 was launched in early 2024 to delve deeper into selected use cases from Phase 1 and explore new use cases. Research on the e-HKD will continue, which will facilitate our study on the possible implementation of e-HKD. For e-CNY, the use of the FPS for topping up e-CNY wallets was successfully tested. We will continue to work with the Digital Currency Institute of the People's Bank of China to further expand the scope of the cross-boundary e-CNY pilot in Hong Kong.

Chief Executive's Statement

The year 2023 marked the fifth anniversary of the FPS and we were able to celebrate it with an important milestone: the FPS x PromptPay link between Hong Kong and Thailand was launched. Hong Kong residents are now able to make retail payments with the FPS in Thailand, while visitors from Thailand can similarly use their faster payment system, PromptPay, to pay for goods and services in Hong Kong. Over these past five years, we have seen the FPS growing both in terms of adoption and applications. The number of FPS registrations increased more than six-fold from more than 2 million at the end of 2018 to reach 13.6 million at the end of 2023, marking an average annual growth of 46%. The FPS also expanded its reach from person-to-person payments to merchant payments, and now to cross-border payments. I am sure our FPS journey will continue, supporting further payment innovations.

Commercial Data Interchange (CDI), a major financial data infrastructure initiative under the "Fintech 2025" strategy which facilitates banks' credit assessments by offering easier access to corporates' business data, has also made significant headway. Since its launch in October 2022, CDI has facilitated more than 13,000 loan applications and reviews, with estimated credit approvals exceeding HK$11.7 billion as at the end of 2023. A linkage was successfully established between CDI and the Government's Consented Data Exchange Gateway late last year to facilitate data sharing between Government departments and financial institutions. The Companies Registry became the first Government data source for CDI, enabling banks to obtain company particulars in a straight-through manner, thereby further digitising and streamlining the KYC ("know your customer") process.

Virtual assets are a rapidly advancing space in the fintech universe, carrying with them both risk and opportunity. Considering the potential financial stability implications of market shocks in the virtual asset sector being transmitted to the traditional financial sector through stablecoins, Hong Kong has kick-started the development of stablecoin regulation, in line with recommendations of international regulatory bodies. Taking into account the initial feedback received from an earlier discussion paper in 2022, the Financial Services and the Treasury Bureau and the HKMA issued a public consultation paper in December 2023 on a legislative proposal to implement a new regulatory regime for stablecoin issuers in Hong Kong, with user protection being one of the key focus areas of the proposed regime. A sandbox arrangement was recently introduced, acting as a channel through which the HKMA can communicate its supervisory expectations to potential stablecoin issuers and obtain feedback from them to facilitate subsequent implementation of the regulatory regime.

Hong Kong's financial platform

To support the stability and effective operation of Hong Kong's financial markets and to help Hong Kong stay competitive globally, the HKMA as regulator and facilitator has over the years taken proactive steps to strengthen the city's financial platform. Last year, legislative amendments were made as part of our continuous efforts to strengthen Hong Kong's attractiveness as the family office base of choice in the region by offering more facilitative tax arrangements. Together with other Government agencies, we are also reviewing the existing tax concession measures applicable to funds, family offices and carried interest, with a view to providing even greater incentives for fund managers, family offices and asset owners around the world to establish a presence here or further expand their local operation.

Chief Executive's Statement

As regards bond market development, building on the success of the world's first tokenised government green bond issuance in February 2023, we assisted the Government in issuing another tokenised green bond in four major currencies earlier this year. This is a significant breakthrough as the issuance marked the world's first multi-currency digital green bond. Apart from promoting innovation in Hong Kong's bond market, we have given fresh impetus to our role as a premier bond issuance hub for Mainland local governments and corporates. In 2023, the governments of Hainan province and Shenzhen municipality issued offshore renminbi local government bonds in Hong Kong, for the second and third consecutive year respectively. These issuances, which included blue bonds, green bonds, social bonds and sustainability bonds, further enriched the range of renminbi financial products available in the Hong Kong market. In October 2023, the HKMA and the National Development and Reform Commission signed a Memorandum of Understanding to better support Mainland cross-border financing activities as well as promote the diversified development of Hong Kong's bond market. These are encouraging developments that provide further opportunities for our bond market to flourish. Moreover, with the Financial Secretary's latest announcement to increase the Government borrowing ceiling to HK$500 billion to cover sustainable finance and infrastructure projects, the local bond market is all set to still grow further in breadth and depth in the years ahead.

Exchange Fund — Staying prudent amid turbulence and uncertainties

Steering the Exchange Fund through global political and financial turbulence in 2023 has been challenging, and the investment performance of the Fund experienced some ups and downs along the way. For the year as a whole, the Exchange Fund recorded an investment income of HK$226.0 billion, representing an investment return of 5.5%. We continued during the year to diversify our investments through the Long-Term Growth Portfolio, which had an annualised internal rate of return of 11.8% since inception.

The outlook for 2024 remains highly unpredictable and challenging for the Exchange Fund. Apart from the uncertain US policy rate path, geopolitical tensions, which so far have not shown any signs of abating, will continue to overshadow investment activities. And with major countries bracing for elections, 2024 will be a year characterised by political and market anxieties.

Despite the complex investment environment, the HKMA will continue to adhere to its principle of "capital preservation first while maintaining long-term growth". We will continue to manage the Exchange Fund with prudence and flexibility, implement appropriate defensive measures, and maintain a high degree of liquidity. We will also step up efforts to incorporate ESG elements into our investment approach as we work towards the target of net-zero greenhouse gas emissions by 2050 for the Investment Portfolio. Details of our progress in the responsible investment journey can be found in our *Sustainability Report 2023*.

Chief Executive's Statement

Looking ahead with vigilance and confidence

It was shortly after I took on my present role in 2019 that the global COVID-19 pandemic broke out. The subsequent three years of shutdown, coupled with the fallout from the 2019 social unrest, dealt an unprecedented blow to the Hong Kong economy. Yet, it is probably fair to say that the three decades since the establishment of the HKMA in 1993 have been dotted with similar stresses and upheavals of various kinds including the 1998 Asian financial crisis, the 2003 SARS outbreak and the 2008 Global Financial Crisis. Each and every time, Hong Kong has demonstrated its ability to bounce back and emerge stronger. It has never been a question of whether, but a matter of when, and in what better shape.

We do not have a crystal ball, and shocks may arise at any time in the global macro environment and financial markets. That is why the HKMA continuously takes proactive, preventive and prudent steps in the discharge of its duties in promoting the stability and integrity of our financial and banking systems, as well as in the management of the Exchange Fund. Looking ahead our dedicated HKMA team will remain vigilant in their service of Hong Kong and in their aim to uphold monetary and banking stability. We shall continue to push boundaries for market development across the key areas of strategic focus to elevate further our status as a leading IFC, always with the same unwavering commitment and optimism that have defined the HKMA since its birth.

Eddie Yue
Chief Executive