

CHAPTER 4 : THE FINANCIAL SECTOR[#]

Summary

- *The low interest rate environment in Hong Kong continued in the first quarter of 2016 amid the accommodative monetary policy in the United States. The Hong Kong dollar interbank interest rates continued to stay at low levels.*
- *The Hong Kong dollar spot exchange rate weakened visibly against the US dollar in January in face of widened negative interest rate differential against the US dollar and heightened volatilities in the global financial markets. It has then strengthened gradually since February upon improved sentiment in the financial markets.*
- *As the US dollar weakened against most major currencies, the trade-weighted Hong Kong dollar Nominal and Real Effective Exchange Rate Indices declined during the first quarter.*
- *Weighed by a weaker economic outlook and a decline in cross-border lending, total loans and advances fell by 0.2% during the first quarter, the third consecutive quarter of decline. Within the total, while loans for use in Hong Kong edged up by 0.1%, loans for use outside Hong Kong declined further by 0.8%.*
- *The local stock market came under further pressure in early 2016, amid concerns over further US interest rate hike and subdued global economic outlook. The Hang Seng Index declined by 5.2% from end-2015 to 20 777 at end-March 2016. Trading activities showed some stabilisation in the first quarter, while fund raising activities cooled off visibly.*

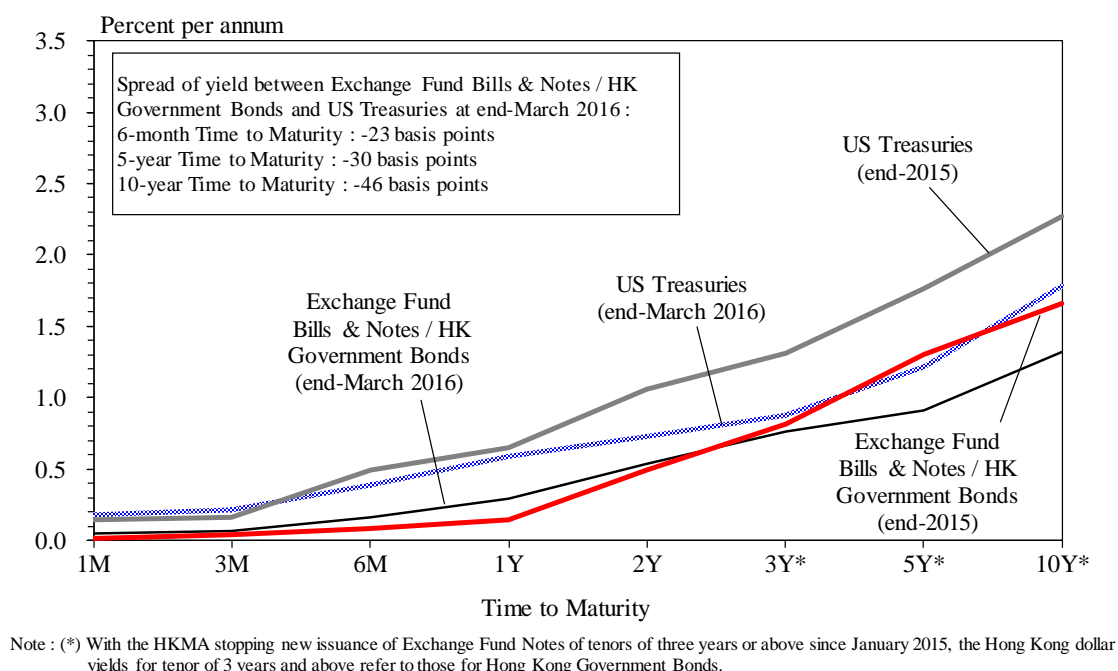
(#) *This chapter is jointly prepared by the Hong Kong Monetary Authority (HKMA) and the Economic Analysis Division.*

Interest rates and exchange rates

4.1 The low interest rate environment in Hong Kong continued in the first quarter of 2016 amid the ongoing accommodative monetary policy in the United States. With the target range for the Federal Funds Rate staying at 0.25-0.75%, the *Base Rate* under the Discount Window operated by the HKMA held unchanged at 0.75% during the quarter⁽¹⁾. The *Hong Kong dollar interbank interest rates* (HIBORs) remained at low levels. While the overnight HIBOR edged up from 0.05% at end-2015 to 0.09% at end-March 2016, and the three-month HIBOR from 0.39% to 0.56%, these were still low levels by historical standards.

4.2 Both the *Hong Kong dollar* and *US dollar yield curves* flattened in the first quarter of 2016. Reflecting the larger declines in US dollar yields, the negative yield spread between 10-year Hong Kong Government Bonds and 10-year US Treasury Notes narrowed from 61 basis points at end-2015 to 46 basis points at end-March 2016, and the negative yield spread between 6-month Exchange Fund Bills and 6-month US Treasury Bills also decreased from 41 basis points to 23 basis points.

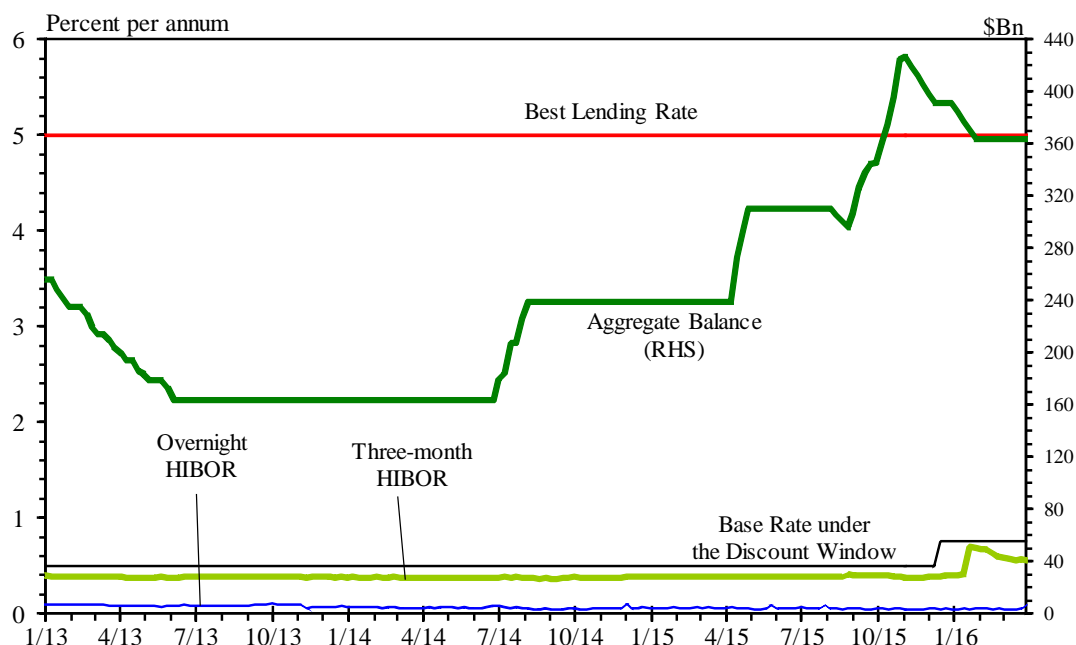
Diagram 4.1 : Both the US dollar and the Hong Kong dollar yield curves flattened in the first quarter of 2016



4.3 Interest rates on the retail front also stayed at low levels. The *Best Lending Rates* remained unchanged at 5.00% or 5.25% in the first quarter. The *average savings deposit rate* stayed low at 0.01% at end-March 2016, while the one-year *time deposit rate* quoted by the major banks for deposits of less

than \$100,000 edged up from 0.14% at end-2015 to 0.15% at end-March 2016. The *composite interest rate*⁽²⁾, which indicates the average cost of funds for retail banks, remained unchanged at 0.26% at end-March 2016.

**Diagram 4.2 : Hong Kong dollar interest rates remained low
(end for the week)**



4.4 The *Hong Kong dollar spot exchange rate* moved within 7.750-7.830 against the US dollar during the first quarter. In January, the Hong Kong dollar weakened visibly against the US dollar in face of widened negative Hong Kong dollar-US dollar interest rate spreads and heightened volatilities in the global financial markets. It has then strengthened gradually since February upon improved sentiment in the financial markets. It closed the quarter at 7.754 per US dollar, compared with 7.751 at end-2015.

4.5 The *Hong Kong dollar forward rates* also witnessed noticeable fluctuations during the first quarter. In late January, the 3-month and 12-month Hong Kong dollar forward rates registered large premiums of 85 pips and 650 pips (each pip equivalent to HK\$0.0001) respectively over the Hong Kong dollar spot rates, partly due to investors' currency hedging activities for their Hong Kong equity portfolios. The premiums then narrowed along with the strengthening of the Hong Kong dollar spot exchange rate. The 3-month forward rate reverted to a discount of 43 pips at end-March while the 12-month forward rate closed at a small premium of 20 pips, compared with the respective discounts of 51 pips and 125 pips at end-2015.

4.6 Under the Linked Exchange Rate System, movements of the Hong Kong dollar exchange rate against other currencies closely followed those of the US dollar. As the US dollar weakened against most major currencies including the Japanese yen, euro and renminbi, the *trade-weighted Hong Kong dollar Nominal and Real Effective Exchange Rate Indices*⁽³⁾ decreased by 1.1% and 0.7% respectively during the first quarter.

Diagram 4.3 : Hong Kong dollar weakened against US dollar in January before strengthening gradually since February (end for the week)

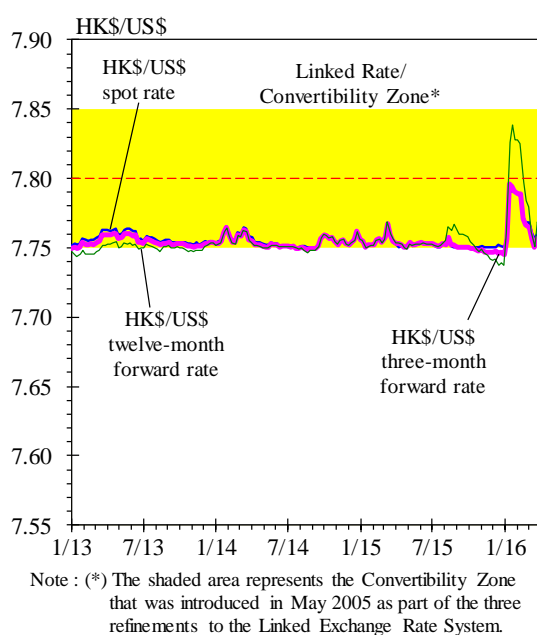
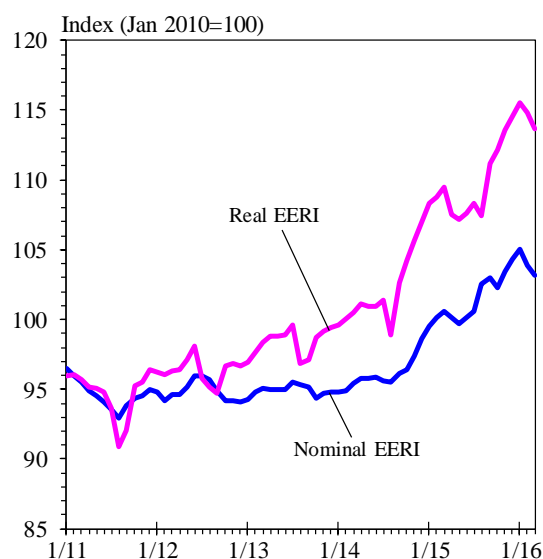


Diagram 4.4 : The trade-weighted nominal and real EERIs declined during the first quarter (average for the month)



Money supply and banking sector

4.7 The monetary aggregates continued to expand at a modest pace in the first quarter of 2016. The Hong Kong dollar broad *money supply* (HK\$M3) increased by 0.6% over end-2015 to \$5,814 billion⁽⁴⁾ at end-March 2016, and the seasonally adjusted Hong Kong dollar narrow money supply (HK\$M1) by 2.5% to \$1,293 billion. Meanwhile, *total deposits* with authorized institutions (AIs)⁽⁵⁾ rose by 2.1% to \$10,971 billion, with Hong Kong dollar and foreign currency deposits increasing by 0.8% and 3.3% respectively.

Diagram 4.5 : The monetary aggregates continued to expand at a modest pace in the first quarter of 2016

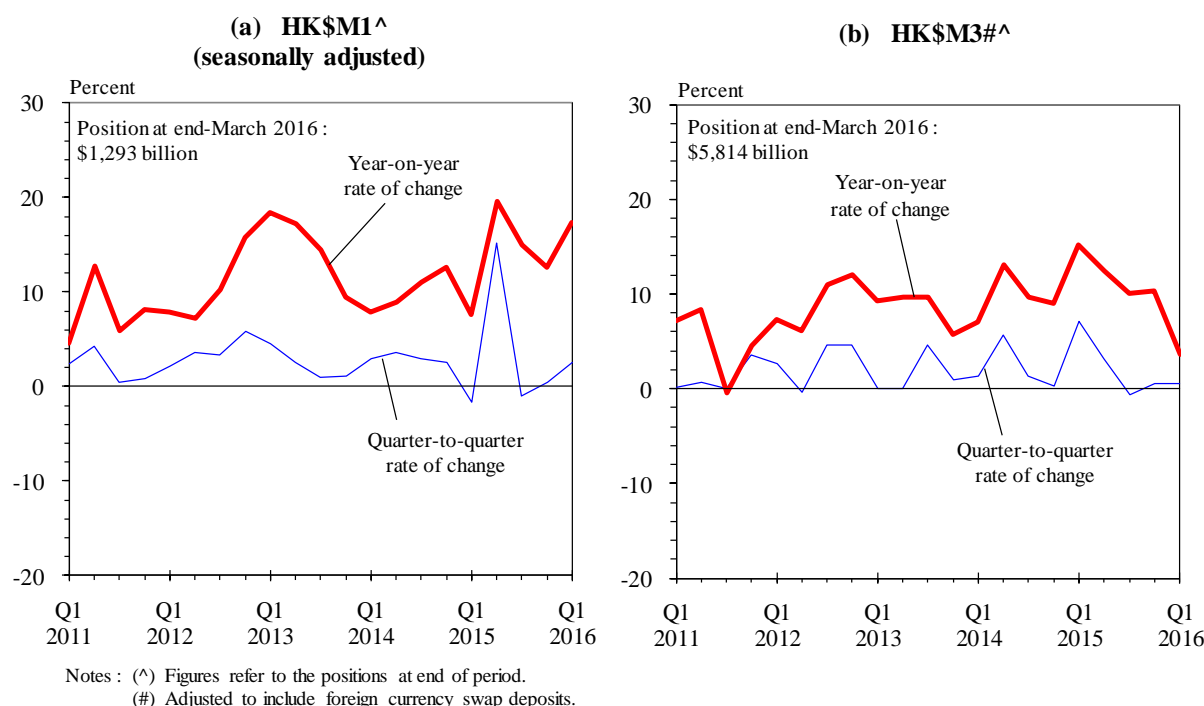


Table 4.1 : Hong Kong dollar money supply and total money supply

		<u>M1</u>		<u>M2</u>		<u>M3</u>	
% change during the quarter		<u>HK\$[^]</u>	<u>Total</u>	<u>HK\$^(a)</u>	<u>Total</u>	<u>HK\$^(a)</u>	<u>Total</u>
2015	Q1	-1.6	13.6	7.2	3.0	7.2	3.0
	Q2	15.2	-1.3	3.1	0.8	3.1	0.8
	Q3	-1.1	5.3	-0.6	0.1	-0.7	0.1
	Q4	0.4	-2.4	0.5	1.5	0.5	1.5
2016	Q1	2.5	5.4	0.6	1.1	0.6	1.1
Total amount at end-March 2016 (\$Bn)		1,293	2,077	5,802	11,748	5,814	11,783
% change over a year earlier		17.3	7.0	3.6	3.5	3.6	3.6

Notes : (^) Seasonally adjusted.

(a) Adjusted to include foreign currency swap deposits.

4.8 Weighed by a weaker economic outlook and a decline in cross-border lending, *total loans and advances* decreased for the third consecutive quarter, by 0.2% from end-2015 to \$7,522 billion at end-March 2016. Within the total, while Hong Kong dollar loans registered a mild increase of 0.8%, foreign currency loans declined at an accelerated 1.4%. Reflecting the relative movements in deposits and loans, the loan-to-deposit ratio for Hong Kong dollar stayed at 78.2% at end-March 2016, unchanged from end-2015, while the

loan-to-deposit ratio for foreign currencies decreased from 62.2% to 59.4%.

4.9 Loans for use in Hong Kong (including trade finance) edged up by 0.1% over end-2015 to \$5,260 billion at end-March 2016. Meanwhile, loans for use outside Hong Kong decreased further by 0.8% to \$2,263 billion. Within the loans for use in Hong Kong, trade finance fell further by 1.5% amid the continued sluggishness in external trade. Dragged by the weak economic growth, loans to wholesale and retail trade and to manufacturing dropped by 6.3% and 2.9% respectively. Loans to financial concerns decreased by 3.6%, though loans to stockbrokers expanded by 7.8%. As for property-related lending, loans to building, construction, property development and investment rebounded by 2.7%, while the growth in loans for purchase of residential property moderated further to 0.5% amid the property market consolidation.

Table 4.2 : Loans and advances

All loans and advances for use in Hong Kong

		Loans to :									
% change during the quarter		Trade finance	Manu- facturing	Whole- sale and retail trade	Building, construction, property development and investment	Purchase of residential property ^(a)	Financial concerns	Stock- brokers	Total ^(b)	All loans and advances for use outside Hong Kong ^(c)	Total loans and advances
2015	Q1	4.2	-3.8	1.0	1.3	2.7	-0.5	338.7	5.6	3.2	4.8
	Q2	0.7	-0.2	-1.5	4.1	1.7	4.8	-55.2	-0.5	3.4	0.6
	Q3	-11.6	0.0	-2.1	2.5	3.0	0.3	-53.3	-1.3	-2.0	-1.5
	Q4	-9.8	-4.3	-3.6	-0.6	1.0	11.5	17.8	0.2	-1.6	-0.3
2016	Q1	-1.5	-2.9	-6.3	2.7	0.5	-3.6	7.8	0.1	-0.8	-0.2
Total amount at end-March 2016 (\$Bn)		447	237	416	1,169	1,125	436	60	5,260	2,263	7,522
% change over a year earlier		-20.9	-7.4	-12.9	8.9	6.4	13.0	-73.4	-1.5	-1.1	-1.4

Notes : Some loans have been reclassified. As such, the figures are not strictly comparable with those of previous quarters.

(a) Figures also include loans for the purchase of flats under the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme, in addition to those for the purchase of private residential flats.

(b) Loans to individual sectors may not add up to all loans and advances for use in Hong Kong, as some sectors are not included.

(c) Also include loans where the place of use is not known.

4.10 The Hong Kong banking sector remains resilient. The Hong Kong incorporated AIs were well capitalised, with the total capital adequacy ratio staying high at 18.3% at end-2015. Meanwhile, asset quality of the local banking sector remains generally healthy. While the ratio of classified loans to total loans increased from 0.56% at end-September 2015 to 0.70% at end-2015⁽⁶⁾, this was still a low level by historical standards. The delinquency ratio for credit card lending hovered at a low level of 0.25% at end-2015, though edging up from 0.24% at end-September. The delinquency ratio for residential mortgage loans rose marginally from 0.03% at end-2015 to 0.04% at end-March 2016.

Table 4.3 : Asset quality of retail banks*

(as % of total loans)

<u>As at end of period</u>		<u>Pass loans</u>	<u>Special mention loans</u>	<u>Classified loans (gross)</u>
2014	Q1	98.42	1.12	0.46
	Q2	98.50	1.05	0.46
	Q3	98.53	1.04	0.43
	Q4	98.44	1.10	0.46
2015	Q1	98.39	1.14	0.46
	Q2	98.23	1.28	0.49
	Q3	98.08	1.36	0.56
	Q4 [^]	97.86	1.44	0.70

Notes : Due to rounding, figures may not add up to 100.

(*) Period-end figures relate to Hong Kong offices and overseas branches. Loans and advances are classified into the following categories: Pass, Special Mention, Substandard, Doubtful and Loss. Loans in the substandard, doubtful and loss categories are collectively known as “classified loans”.

([^]) Figures prior to December 2015 cover retail banks’ Hong Kong offices and overseas branches. Starting from December 2015, the coverage was expanded to include the banks’ major overseas subsidiaries.

4.11 *Offshore renminbi (RMB) business* showed some consolidation in the first quarter amid some fluctuations in the RMB market and change in expectation for RMB exchange rate. Total RMB deposits (including customer deposits and outstanding certificates of deposit) decreased by 12.1% from end-2015 to RMB888.4 billion at end-March 2016. In the first quarter of 2016, RMB trade settlement transactions handled by banks in Hong Kong plunged by 30.5% from a year earlier or 28.8% from the preceding quarter to RMB1,130.6 billion. RMB financing activities also softened. RMB bond issuance plunged from RMB21.6 billion in the preceding quarter to RMB4.3 billion in the first quarter. RMB bank lending declined by 5.3% from end-2015 to RMB281.6 billion at end-March 2016.

Table 4.4 : Renminbi deposits and cross-border renminbi trade settlement in Hong Kong

As at end of period		Interest rates on ^(a)					Number of AIs engaged in RMB business	Amount of cross-border RMB trade settlement ^(c) (RMB Mn)
		Demand and savings deposits (RMB Mn)	Time deposits (RMB Mn)	Total deposits (RMB Mn)	Savings deposits ^(b) (%)	Three-month time deposits ^(b) (%)		
2015	Q1	157,444	794,550	951,994	0.25	0.53	147	1,626,122
	Q2	180,445	812,479	992,924	0.25	0.53	146	1,569,670
	Q3	165,849	729,516	895,365	0.25	0.53	145	2,050,107
	Q4	160,908	690,198	851,106	0.25	0.53	145	1,587,184
2016	Q1	187,124	572,302	759,425	0.25	0.53	145	1,130,645
% change in 2016 Q1 over 2015 Q1		18.9%	-28.0%	-20.2%	N.A.	N.A.	N.A.	-30.5%
% change in 2016 Q1 over 2015 Q4		16.3%	-17.1%	-10.8%	N.A.	N.A.	N.A.	-28.8%

Notes : (a) The interest rates are based on a survey conducted by the HKMA.

(b) Period average figures.

(c) Figures during the period.

N.A. Not available.

The debt market

4.12 The Hong Kong dollar *debt market* expanded further in the first quarter of 2016. Total gross issuance of Hong Kong dollar debt securities rose by 2.9% over the preceding quarter to \$709.1 billion, underpinned by an increase in issuance by both the private and public sectors. Specifically, debt issuance by the private sector expanded by 14.8%, mainly driven by a surge in issuance by AIs⁽⁷⁾. Debt issuance by the public sector recorded a modest growth of 1.5%, with the increase in new debts issued by the Exchange Fund and statutory bodies/government-owned corporations more than offsetting the decrease in government bond issuance. Against this backdrop, the total outstanding balance of Hong Kong dollar debt securities rose by another 2.1% over end-2015 to \$1,556.5 billion at end-March 2016, equivalent to 26.8% of HK\$M3 or 22.4% of Hong Kong dollar-denominated assets of the entire banking sector⁽⁸⁾.

4.13 As to the Government Bond (“GB”) Programme, a total of \$1.6 billion institutional GBs were issued through tenders in the first quarter. At end-March, the total outstanding amount of Hong Kong dollar bonds under the GB programme was \$100.5 billion, comprising 14 institutional issues totaling

\$70.5 billion and three retail issues (iBonds) totaling \$30 billion. In addition, there were two outstanding US dollar sukuks, each with an issuance size of US\$1 billion.

4.14 The Financial Secretary announced in the 2016-17 Budget that the Government would launch another iBond issue of up to \$10 billion with a maturity period of three years, same as the previous issuances. Also, the Government would launch a pilot scheme to issue Silver Bond this year and next year, also an inflation-linked bond but targeting at Hong Kong residents aged 65 or above, with a maturity of three years for the first issuance.

**Table 4.5 : New issuance and outstanding value of
Hong Kong dollar debt securities (\$Bn)**

		<u>Exchange Fund paper</u>	<u>Statutory bodies/govern- ment-owned corporations</u>	<u>Govern- ment</u>	<u>Public sector total</u>	<u>AIs^(a)</u>	<u>Local corporations</u>	<u>Non-MDBs overseas borrowers^(b)</u>	<u>Private sector total</u>	<u>MDBs^(b)</u>	<u>Total</u>
New Issuance											
2015	Annual	2,242.2	12.0	30.4	2,284.6	136.4	14.2	58.9	209.4	0.0	2,494.0
	Q1	491.9	4.3	7.9	504.1	54.4	4.4	10.6	69.4	0.0	573.5
	Q2	541.2	4.0	4.7	550.0	23.2	2.1	15.5	40.8	0.0	590.7
	Q3	599.9	0.8	10.6	611.3	14.8	2.8	12.0	29.6	0.0	641.0
	Q4	609.1	2.9	7.2	619.2	44.0	4.9	20.7	69.6	0.0	688.8
2016	Q1	622.4	4.4	1.6	628.4	53.8	4.7	21.4	79.9	0.8	709.1
% change in 2016 Q1 over 2015 Q1		26.5	2.2	-79.7	24.6	-1.1	8.3	101.5	15.2	N.A.	23.6
% change in 2016 Q1 over 2015 Q4		2.2	53.1	-77.8	1.5	22.2	-3.5	3.4	14.8	N.A.	2.9
Outstanding (as at end of period)											
2015	Q1	752.8	43.5	105.9	902.2	249.7	140.3	142.4	532.4	6.1	1,440.7
	Q2	753.0	43.2	94.1	890.3	245.9	140.1	148.5	534.5	5.3	1,430.1
	Q3	773.2	43.2	104.7	921.1	230.7	141.1	152.2	524.1	5.3	1,450.5
	Q4	828.4	44.1	100.4	972.9	242.6	141.7	162.1	546.4	5.3	1,524.6
2016	Q1	856.9	47.3	102.0	1,006.2	232.5	142.1	169.7	544.4	6.0	1,556.5
% change in 2016 Q1 over 2015 Q1		13.8	8.6	-3.7	11.5	-6.9	1.3	19.2	2.2	-2.3	8.0
% change in 2016 Q1 over 2015 Q4		3.4	7.4	1.6	3.4	-4.1	0.3	4.7	-0.4	12.5	2.1

Notes : Figures may not add up to the corresponding totals due to rounding and may be subject to revisions.

N.A. Not available.

(a) AIs : Authorised institutions.

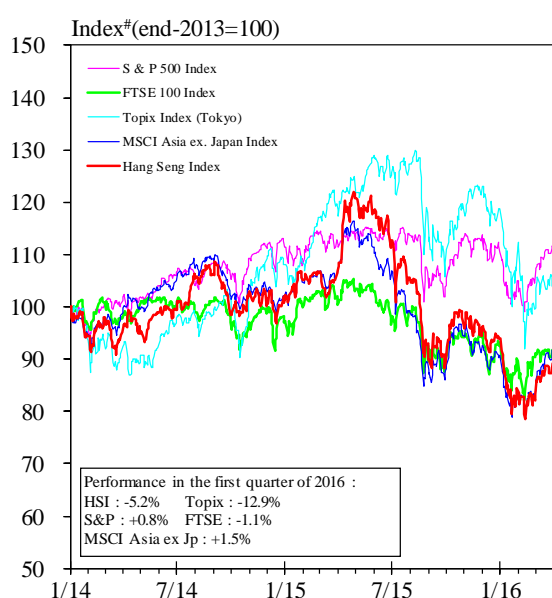
(b) MDBs : Multilateral Development Banks.

The stock and derivatives markets

4.15 After a weak performance in the second half of 2015, the *local stock market* came under further pressure in early 2016. Plagued by concerns over further US interest rate hike and subdued global economic outlook, the Hang Seng Index (HSI) plunged to 18 320 on 12 February, the lowest level since June 2012. While recouping some of the loss in the latter part of the quarter amid easing concerns over US rate hike, the HSI still declined by 5.2% from end-2015 to 20 777 at end-March 2016. In parallel, the *market capitalisation* declined by 5.0% to \$23.4 trillion. The local stock market was the seventh largest stock exchange in the world and third largest in Asia⁽⁹⁾.

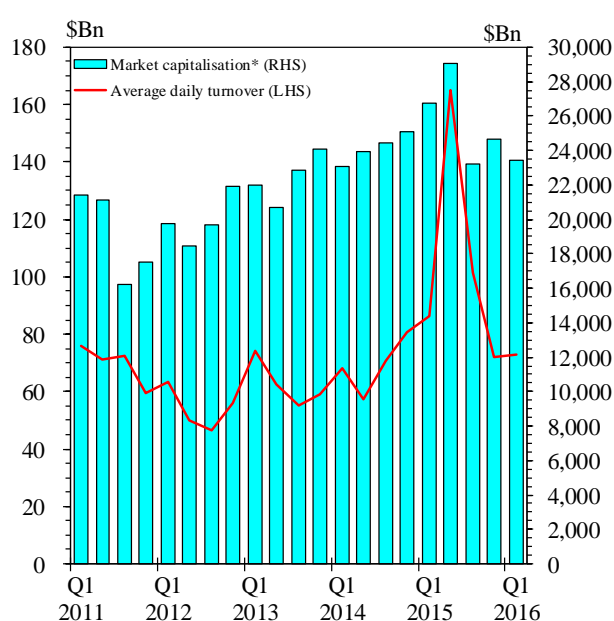
4.16 Following a visible contraction in the two preceding quarters, trading activities showed some stabilisation in the first quarter. *Average daily turnover* in the securities market edged up by 1.1% over the preceding quarter to \$72.7 billion, though representing a decline of 15.9% from a year earlier. Trading for different types of securities showed a mixed performance. Average daily trading value of equities declined by 2.8% from the preceding quarter. Average daily trading value of derivative warrants and unit trusts (including Exchange-Traded Funds) jumped by 23.1% and 15.6% respectively, while that of callable bull/bear contracts declined by 19.6%⁽¹⁰⁾ (**Box 4.1**). As to futures and options⁽¹¹⁾, the average daily trading volume surged by 25.5%. Within the total, the trading of HSI options, HSI futures, H-shares Index futures and stock options all grew notably, by 48.5%, 23.6%, 22.9% and 21.5% respectively.

Diagram 4.6 : The local stock market came under further pressure in early 2016



Note : (#) Position at end of month.

Diagram 4.7 : Market capitalisation declined, while trading activities showed some stabilisation



Note : (*) Position at end of quarter.

**Table 4.6 : Average daily turnover of futures and options
of the Hong Kong market**

		Hang Seng Index <u>futures</u>	Hang Seng Index <u>options</u>	H-shares <u>Index futures</u>	Stock <u>options</u>	Total futures and <u>options traded*</u>
2015	Annual	85 991	30 427	135 139	374 346	768 520
	Q1	64 351	27 727	108 774	363 322	672 678
	Q2	81 541	35 129	154 553	523 860	946 336
	Q3	82 744	33 238	152 006	375 780	819 085
	Q4	114 430	25 752	125 310	241 192	641 404
2016	Q1	141 439	38 235	154 053	293 047	805 276
% change in 2016 Q1 over 2015 Q1		119.8	37.9	41.6	-19.3	19.7
% change in 2016 Q1 over 2015 Q4		23.6	48.5	22.9	21.5	25.5

Notes : (*) Turnover figures for individual futures and options are in number of contracts, and may not add up to the total futures and options traded as some products are not included.

4.17 Due to the nature of business, fund raising activities are inherently volatile. *Total equity capital raised*, comprising new share floatation and post-listing arrangements on the Main Board and the Growth Enterprise Market (GEM)⁽¹²⁾, plunged by 69.6% from the high base in the preceding quarter or 4.7% from a year earlier to \$80.2 billion in the first quarter. Within the total, the amount of funds raised through Initial Public Offerings (IPOs) plummeted by 73.8% from the preceding quarter to \$28.0 billion. Nonetheless, Hong Kong still ranked the third globally in terms of the funds raised through IPOs in the first quarter.

Box 4.1

Cash Market Transaction Survey 2014/15

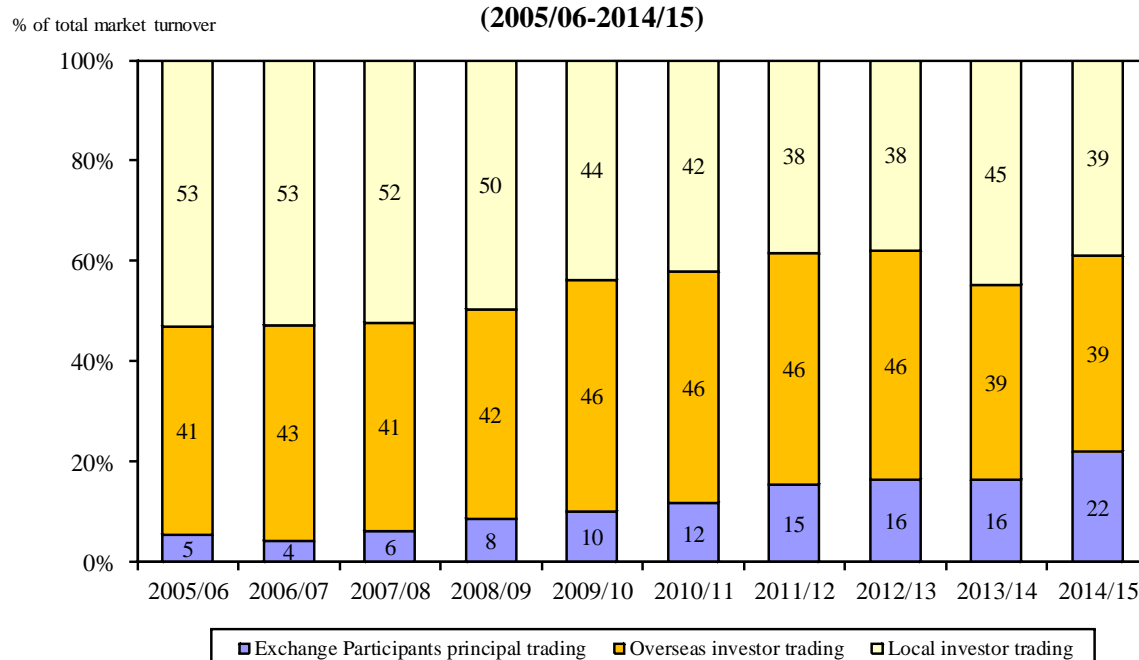
The securities market in Hong Kong is renowned for the active participation of different types of investors from a great variety of origins. To better understand the trading composition, the Hong Kong Exchanges and Clearing Limited (HKEX) has been conducting an annual survey on investor profile since 1991. The latest issue, “Cash Market Transaction Survey 2014/15”, covered HKEX’s securities market turnover from October 2014 to September 2015 and was published in February 2016. The latest survey also included the Southbound trading through Shanghai-Hong Kong Stock Connect (“Stock Connect”), which was launched on 17 November 2014. Some salient observations are summarised below.

(1) Overall trading and trading by investor type

Trading activities in the securities market were very hectic in 2014/15. Total turnover reached a record high of \$26.6 trillion, a surge of 68% over the preceding year and surpassing the peak in 2007/08 by 16%. Trading by all major investor types recorded significant growth, led by a leap of 124% in Exchange Participants (EP) principal trading (i.e. trading of the participant firm’s own account). Overseas and local investor trading also rose sharply, by 71% and 45% respectively.

Indeed, in the past ten years, EP principal trading generally grew faster than trading by the other two types of investors. Between 2005/06 and 2014/15, EP principal trading recorded an average annual growth of 36%, sharply above the respective average annual growth of 16% and 12% for overseas and local investor trading. As a result, the share of EP principal trading rose from a mere 5% in 2005/06 to 22% in 2014/15. Meanwhile, the share of overseas investor trading declined from 41% to 39%, and that of local investor trading from a high of 53% to 39%.

**Chart 1 : Distribution of securities market trading value by investor type
(2005/06-2014/15)**

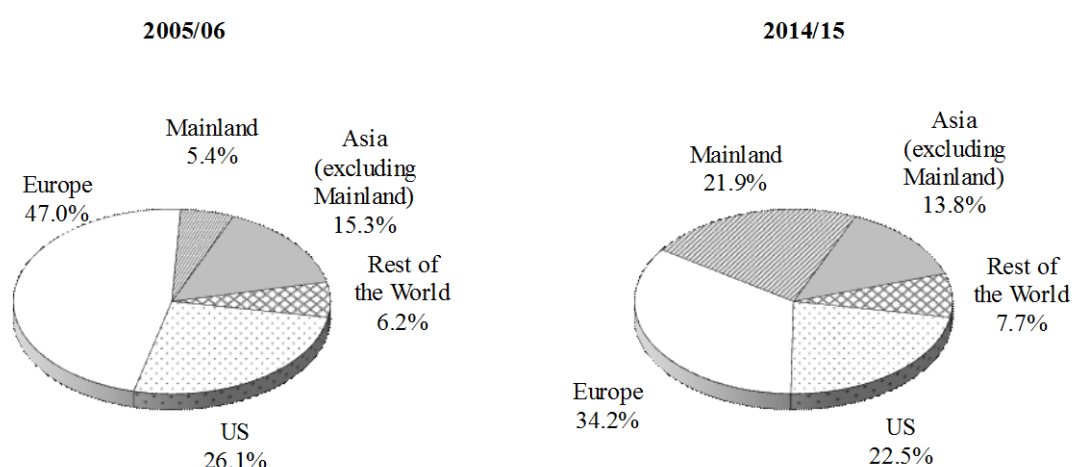


Box 4.1 (Cont'd)

(2) Overseas investors by origin

Mainland investors have been the major growth impetus for overseas investor trading in 2014/15, partly reflecting the launch of the Stock Connect in November 2014. In 2014/15, trading by Mainland investors soared by 185%, while trading by investors from other origins registered diverged growth of 13% to 120%. In tandem with the faster increase in the past ten years, the share of Mainland investors in total overseas investor trading ballooned from 5% in 2005/06 to 22% in 2014/15. While the shares of US and European investors together still accounted for 57% in 2014/15, this represented a visible retreat from the 73% a decade ago.

Chart 2 : Distribution of overseas investor trading in the securities market by origin



Note: Figures may not add up to 100 due to rounding.

(3) Retail online trading

Online trading has become a popular way of trading securities among retail investors in Hong Kong, facilitated by several factors including technological improvement and enhanced cyber-security. Total trading value of retail online trading reached \$3.1 trillion in 2014/15, a spectacular growth of 110% over a year earlier. During the period from 2005/06 to 2014/15, retail online trading recorded an average growth of 31% per annum, much higher than that of 9% for retail non-online trading. It accounted for 44% of total retail investor trading in 2014/15, up from only 13% in 2005/06.

4.18 Mainland enterprises continued to play a dominant role in the Hong Kong stock market. At end-March 2016, a total of 962 Mainland enterprises (including 231 H-share companies, 151 “Red Chips” companies and 580 private enterprises) were listed on the Main Board and GEM, accounting for 51% of the total number of listed companies and 62% of total market capitalisation. In the first quarter, Mainland-related stocks accounted for 70% of equity turnover and 60% of total equity fund raised in the Hong Kong stock exchange.

4.19 Following an earlier public consultation, in February the Securities and Futures Commission (SFC) proposed to expand the scope of short position reporting to all securities that can be short sold under the rules of The Stock Exchange of Hong Kong Limited including collective investment schemes⁽¹³⁾. The new reporting arrangement would help improve market surveillance and transparency, and thus be conducive to the long-term development of the securities market and financial industry. The new reporting arrangement will come into effect in March 2017.

4.20 Separately, in February the HKMA and the SFC announced the revised proposals for introducing the first phase of mandatory clearing and the second phase of mandatory reporting under the over-the-counter derivatives regimes. The revisions are pertinent to the coverage and the commencement dates of the regimes, and are made in response to the comments received during the earlier consultation. The first phase of mandatory clearing will commence on 1 September 2016, and the second phase of mandatory reporting on 1 July 2017.

Fund management and investment funds

4.21 Performance of different segments in the fund management business was mixed in the first quarter. While the monthly average gross retail sales of *mutual funds* rose by 15.7% over the low base in the fourth quarter of 2015 to US\$4.3 billion in January – February 2016⁽¹⁴⁾, this represented a plunge of 38.2% from a year earlier. Meanwhile, the aggregate net asset value of the approved constituent funds under the *Mandatory Provident Fund (MPF) schemes*⁽¹⁵⁾ edged up by 0.2% from end-2015 to \$592.6 billion at end-March 2016. The amount of net assets managed by *retail hedge funds* rebounded⁽¹⁶⁾.

Insurance sector

4.22 The *insurance sector*⁽¹⁷⁾ expanded further in 2015. Gross premium income from long-term business jumped by 15.1%, though the performances varied across different segments. Premium income from non-investment linked plans surged by 23.7%, while that from investment-linked plans plunged by 36.2%, mainly dragged by a contraction in the second half amid the global stock market correction. Meanwhile, gross and net premium for general business rose modestly, by 4.7% and 5.9% respectively.

Table 4.7 : Insurance business in Hong Kong* (\$Mn)

		General business			Premium for long-term business^					Gross premium from long-term business and general business
		Gross premium	Net premium	Underwriting profit	Individual life and annuity (non-linked)	Individual life and annuity (linked)	Other individual business	Non-retirement scheme group business	All long-term business	
2014	Annual	43,896	30,299	3,010	97,357	16,052	176	451	114,036	157,932
	Q1	12,551	8,668	902	23,770	3,387	39	180	27,376	39,927
	Q2	10,642	7,697	636	23,191	4,210	40	53	27,494	38,136
	Q3	11,534	7,936	853	24,652	4,317	47	120	29,136	40,670
	Q4	9,169	5,998	619	25,744	4,138	50	98	30,030	39,199
2015	Annual	45,961	32,085	1,697	120,435	10,243	178	417	131,273	177,234
	Q1	12,939	9,053	645	32,060	4,249	52	121	36,482	49,421
	Q2	10,943	7,888	58	28,909	3,210	42	80	32,241	43,184
	Q3	11,592	7,900	803	27,356	1,328	43	145	28,872	40,464
	Q4	10,487	7,244	191	32,110	1,456	41	71	33,678	44,165
% change in 2015 Q4 over 2014 Q4		14.4	20.8	-69.1	24.7	-64.8	-18.0	-27.6	12.1	12.7
% change in 2015 over 2014		4.7	5.9	-43.6	23.7	-36.2	1.1	-7.5	15.1	12.2

Notes : (*) Figures are based on provisional statistics of the Hong Kong insurance industry.

(^) Figures refer to new business only. Retirement scheme business is excluded.

Notes :

- (1) Prior to 9 October 2008, the Base Rate was set at either 150 basis points above the prevailing US Federal Funds Target Rate (FFTR) or the average of the five-day moving averages of the overnight and one-month HIBORs, whichever was higher. Between 9 October 2008 and 31 March 2009, this formula for determination of the Base Rate was temporarily changed by reducing the spread of 150 basis points above the prevailing FFTR to 50 basis points and by removing the other leg relating to the moving averages of the relevant interbank interest rates. After a review of the appropriateness of the new Base Rate formula, the narrower 50 basis point spread over the FFTR was retained while the HIBOR leg was re-instated in the calculation of the Base Rate after 31 March 2009.
- (2) In December 2005, the HKMA published a new data series on composite interest rate, reflecting movement in various deposit rates, interbank and other interest rates to closely track the average cost of funds for banks. The published data enable the banks to keep track of changes in funding cost and thus help improve interest rate risk management in the banking sector.
- (3) The trade-weighted Nominal Effective Exchange Rate Index (EERI) is an indicator of the overall exchange value of the Hong Kong dollar against a fixed basket of other currencies. Specifically, it is a weighted average of the exchange rates of the Hong Kong dollar against some 15 currencies of its major trading partners, with the weights adopted being the respective shares of these trading partners in the total value of merchandise trade for Hong Kong during 2009 and 2010.

The Real EERI of the Hong Kong dollar is obtained by adjusting the Nominal EERI for relative movements in the seasonally adjusted consumer price indices of the respective trading partners.

- (4) The various definitions of the money supply are as follows:

M1 : Notes and coins with the public, plus customers' demand deposits with licensed banks.

M2 : M1 plus customers' savings and time deposits with licensed banks, plus negotiable certificates of deposit (NCDs) issued by licensed banks, held outside the monetary sector as well as short-term Exchange Fund placements of less than one month.

M3 : M2 plus customers' deposits with restricted licence banks and deposit-taking companies, plus NCDs issued by such institutions and held outside the monetary sector.

Among the various monetary aggregates, more apparent seasonal patterns are found in HK\$M1, currency held by the public, and demand deposits.

- (5) AIs include licensed banks, restricted licence banks and deposit-taking companies. At end-March 2016, there were 157 licensed banks, 24 restricted licence banks and 18 deposit-taking companies in Hong Kong. Altogether, 199 AIs (excluding representative offices) from 30 countries and territories (including Hong Kong) had a presence in Hong Kong.

- (6) Figures prior to December 2015 are related to retail banks' Hong Kong offices and overseas branches. Starting from December 2015, the coverage was expanded to include locally incorporated retail banks' major overseas subsidiaries. Excluding the major overseas subsidiaries, the classified loan ratio of retail banks was 0.63% at end-2015.
- (7) The figures for private sector debt may not represent a full coverage of all the Hong Kong dollar debt paper issued.
- (8) Assets of the banking sector include notes and coins, amount due from Authorised Institutions in Hong Kong as well as from banks abroad, loans and advances to customers, negotiable certificates of deposit (NCDs) held, negotiable debt instruments other than NCDs held, and other assets. Certificates of indebtedness issued by Exchange Fund and the counterpart bank notes issued are nevertheless excluded.
- (9) The ranking is based on the figures compiled by the World Federation of Exchanges and the London Stock Exchanges Group.
- (10) Given the relatively small share (less than 0.5% of the daily turnover in the securities market), trading of debt securities and its movements were not analysed.
- (11) At end-March 2016, there were 84 classes of stock options contracts and 74 classes of stock futures contracts.
- (12) At end-March 2016, there were 1 656 and 227 companies listed on the Main Board and GEM respectively.
- (13) The existing short position reporting regime, introduced in June 2012, applied only to constituents of HSI and Hang Seng China Enterprises Index and other financial stocks specified by the SFC.
- (14) These figures are obtained from the Sales and Redemptions Survey conducted by the Hong Kong Investment Funds Association on their members, and cover only the active authorised funds that have responded to the survey. At end-February 2016, the survey covered a total of 1 156 active authorised funds.
- (15) At end-March 2016, there were 19 approved trustees. On MPF products, 35 master trust schemes, two industry schemes and one employer sponsored scheme, comprising altogether 462 constituent funds, were approved by the Mandatory Provident Fund Schemes Authority. A total of 276 000 employers, 2.55 million employees and 205 000 self-employed persons have participated in MPF schemes.
- (16) At end-March 2016, there were three SFC-authorised retail hedge funds with combined net asset size of US\$110 million. The amount of net assets under management represented a 29.4% increase from the end-2015 level, and a 31.3% decrease from end-2002, the year when the hedge funds guidelines were first issued.
- (17) At end-March 2016, there were 157 authorised insurers in Hong Kong. Within this total, 45 were engaged in long-term insurance business, 93 in general insurance business, and 19 in composite insurance business. These authorised insurers came from 23 countries and territories (including Hong Kong).