Box 4.1

Development of Exchange-Traded Funds (ETFs) in Hong Kong

An exchange-traded fund (ETF) is a listed open-ended collective investment scheme which tracks the movement of a specific underlying benchmark (e.g. the Hang Seng Index or the price of gold). Given that they can be traded at a stock exchange, ETFs offer investors a liquid and convenient access to a specific sector, stock index or asset class. From a broader perspective, there are also views that ETFs which track a commonly-used market index could facilitate spot-futures arbitrage through reducing the total costs for replicating the index portfolio, and hence could potentially enhance efficiency of the stock market.

The first ETF in Hong Kong was listed in 1999, and was also the first ETF in Asia outside Japan. After a steady development during 2000-2006, the ETF market in Hong Kong has been expanding at a brisk pace since 2007. Taking advantage of the huge opportunities related to the Mainland market, several global ETF managers and issuers have set up and expanded their operation in Hong Kong. The number of ETFs has also witnessed a jump from only one at end-1999 to 69 at end-2010. For the first half of 2011, another seven ETFs were launched, bringing the number of ETFs in Hong Kong to 76 at end-June.

As to trading, ETFs have been gaining popularity among investors in Hong Kong. A survey by the Hong Kong Exchanges and Clearing Limited indicated that around 25% of retail investors have invested in ETFs in 2009\(^1\). In 2010, turnover of ETFs amounted to over $600 billion, accounting for 3.5% of total market turnover. During 2000-2010, average daily turnover of ETFs recorded a spectacular average annual growth of 42%. In consequence to these developments, Hong Kong has become the largest ETF market in terms of total turnover and third largest in terms of number in the Asia-Pacific region in 2010.

Number and average daily turnover of ETFs in Hong Kong

![Number and average daily turnover of ETFs in Hong Kong](chart)

Notes: Figures in brackets represent the average daily turnover of ETFs in Hong Kong as a share of the total in the securities market.\(^(*)\) Position at end of period.

Source: Hong Kong Exchanges and Clearing Limited (HKEx).

\(^1\) “Retail Investor Survey 2009” published in March 2010.
Most ETFs in Hong Kong have equity as the underlying benchmark. A total of 70 out of 76 ETFs at end-June 2011 were designed to track the performance of equity and related indices. Within this, 44 focused on the Greater China market (including Hong Kong, the Mainland and Taiwan), while the remaining 26 covered the rest of the world (e.g. India, Korea, the US). On the other hand, there were six ETFs on fixed income, money market, and commodities and related index.

Looking ahead, Hong Kong would continue to leverage on its financial co-operation with the Mainland and unique role as an offshore renminbi centre for the further development of the ETF market. Specifically, with the signing of the Closer Economic Partnership Arrangement Supplement VI in May 2009 and Supplement VII in May 2010, ETFs on stocks in Hong Kong could be introduced in the Mainland. The Government has been closely liaising with the relevant Mainland authorities on the launch of cross-border ETFs.