The Basic Law also provides for Hong Kong to continue its independent currency system, under which designated banks are authorised to issue local banknotes.

**Hong Kong as an international financial centre**

Hong Kong’s economic prosperity depends very much on its continued success in maintaining its status as an international financial centre. This is Exchange Square.
important not only to Hong Kong, but also to the whole of China, which has been undergoing gradual and steady financial modernisation in tandem with its rising economic power.

That is why Article 109 stipulates that “the Government of the HKSAR shall provide an appropriate economic and legal environment for the maintenance of the status of Hong Kong as an international financial centre”. More specifically, Article 110 provides that “the monetary and financial systems of the HKSAR shall be prescribed by law. The Government of the HKSAR shall, on its own, formulate monetary and financial policies, safeguard the free operation of financial business and financial markets, and regulate and supervise them in accordance with law”.

In this regard, Hong Kong can pride itself on its highly transparent and robust regulatory regime for the banking, securities and futures, insurance and retirement scheme industries, in line with the best global practices and standards. Amongst the principal regulators are the Hong Kong Monetary Authority, Securities and Futures Commission, Office of the Commissioner of Insurance and Mandatory Provident Fund Schemes Authority. Special efforts have also been made to promote corporate governance, investor education and financial co-operation with the Mainland.

As a major international financial centre, Hong Kong has an integrated network of institutions and markets, providing a wide range of financial products and services with a high degree of liquidity to local and international investors. Hong Kong was ranked first among 60 leading financial systems and capital markets in the world in the World Economic Forum’s Financial Development Report 2011. It was the first time an Asian financial centre had received such an honour. Moreover, according to the Global Financial Centres Index 10 released in September 2011, Hong Kong was recognised as the top financial centre in Asia, and came third among 75 major financial centres globally, after London and New York.

The achievements of Hong Kong’s equity market have been equally impressive in terms of market capitalisation and trading turnover after the handover. Its equity market capitalisation reached US$21,077 billion in 2010 - the seventh largest in the world and the third in Asia. Hong Kong led the world in total funds raised through Initial Public Offerings (IPOs) from 2009 to 2011, surpassing London and New York.

As at end 2011, there were 152 licensed banks, 20 restricted licensed banks and 26 deposit-taking companies in Hong Kong. These banking institutions include 73 of the world’s 100 largest banks.

The foreign exchange market of Hong Kong is one of the largest and freest in the world. Ranked among the world’s best, the local debt, insurance, gold and futures markets have all been expanding rapidly.
An offshore Renminbi clearing centre

Another exciting development in Hong Kong’s financial services markets is the gradual and steady internationalisation of the Renminbi (RMB) in tandem with a shift in the centre of economic gravity from the West to the East. Capitalising on the unique advantage of “One Country, Two Systems”, Hong Kong plays an important role as a firewall and testing grounds for the nation in its drive towards RMB internationalisation.

2004 marked the beginning of RMB deposit growth in Hong Kong. RMB remittances, exchange, credit cards and deposits were introduced to the city in that year. Since then, RMB businesses have continued to grow.

In 2007, Hong Kong became the first and only offshore place to have a RMB bond market. The growth rate of Hong Kong’s RMB deposit base started to accelerate with the launch of the trade settlement pilot scheme in July 2009. RMB services in Hong Kong has been extended to cover deposit-taking, currency exchange, remittances, credit and debit cards, cheques, corporate loans, bond issuance and trading, gold trading and trade settlement services. Of the 1,676 billion yuan in China’s RMB trade settlement, some 86% was handled by Hong Kong in the first quarter of 2011. It is clear that Hong Kong has become an offshore RMB centre for Asia and beyond.
Hong Kong also stands to benefit most from the recent move by the CPG to accelerate the pace of internationalising the RMB, including the introduction of Qualified Foreign Institutional Investors, the listing of Hong Kong stocks in the Mainland market through exchange-traded funds as well as the issuance of “dim sum” bonds by the Mainland’s onshore non-financial companies.

It should be noted that Hong Kong’s financial markets have not only become the major fund-raising platform for Mainland enterprises, they are also playing a facilitating role in
helping the latter to improve corporate governance, enhance operational efficiency, promote brand names and globalise their business activities.

With the Mainland replacing Japan as the world’s second largest economy, the process of RMB internationalisation signifies a new era of rapid growth in China’s trade and investment links with the world. Hong Kong stands to be an important part of China’s growth story in this new era.

Economic shocks and recovery

The past 15 years were not without challenges, but Hong Kong has always been able to ride the waves and thrive after severe economic shocks.

The first wave of these shocks was the Asian financial crisis, which quickly spread across Southeast Asia just days after the handover in 1997. Many Asian currencies experienced substantial losses against the US dollar. Hong Kong’s financial markets could not be immune from the crisis, but the speculative attacks and massive short-selling of the Hong Kong dollar and stocks in 1998 were fought off by a HK$118 billion government injection in the stock market and the raising of the overnight rate from 8% to 18%. Although controversial at the time, the market intervention proved to be essential in restoring order and confidence in Hong Kong’s financial markets.

Then came the bursting of the dot.com bubble in 2000, followed by the global economic slowdown of 2001, which hindered Hong Kong’s recovery process.

In the aftermath of these crises, Hong Kong went through several years...
of economic downturn, during which property prices, stocks, consumer goods and wages fell sharply. That difficult period was characterised by a high unemployment rate and closure of companies and shops.

The economy took another blow in 2003 when the city was pummelled by the Severe Acute Respiratory Syndrome (SARS). The deadly infectious disease was a severe blow to the tourism industry and retail business with sharp declines in arrivals from Europe, the United States and other parts of the world. Local consumer sentiment dropped to its lowest ever.

Premier Wen Jiabao visits a family badly hit by SARS in Amoy Gardens.

Primary school pupils washing their hands before class—regular washing of hands was one of many preventive measures adopted throughout the community after SARS struck.

Hong Kong people stoically soldiered on during the epidemic.
Road to recovery

Before long, Hong Kong was on the mend, thanks largely to the Individual Visit Scheme (IVS) introduced by the CPG in 2003 to allow Mainland travellers to visit Hong Kong and Macao on an individual basis. The IVS brought relief to the local retail, hotel and catering industries, benefiting the domestic economy and employment. Another major boost to Hong Kong’s economic recovery was the implementation of the Closer Economic Partnership Arrangement (CEPA) in 2004, which provides local companies and professionals with easier access to the enormous Mainland market.

As a result of the IVS and CEPA, Hong Kong’s economy gradually bounced back in 2004. The economy expanded by a cumulative 48% in real terms during 2004 to 2011, with Gross Domestic Product (GDP) reaching a total of almost HK$1.9 trillion in 2011.

Hong Kong also emerged in good shape from the global financial crisis in 2008, which was triggered by the Lehman Brothers’ bankruptcy. Hong Kong was one of the few economies that managed to recover fully in less than two years. The economy began to rebound in the second quarter of 2009, and was largely back to the pre-crisis peak by the first quarter of 2010. The economy recorded 7% growth in 2010, and further above-trend growth of 5% in 2011. This quick recovery reflects Hong Kong’s resilience and fundamental strengths, in particular its prompt actions which served to stabilise the monetary system,
preserve employment and support enterprises during the crisis. Another crucial factor was the Mainland’s role in helping to cushion an export collapse in Hong Kong with its strong domestic demand.

Leveraging on CEPA

The implementation of CEPA is made possible by the “One Country, Two Systems” principle and the Basic Law, which provides Hong Kong with separate membership in the World Trade Organization (WTO).

CEPA is a win-win agreement, bringing new business opportunities to the Mainland, Hong Kong and all foreign investors. CEPA provides great opportunity for Hong Kong businesses to gain access to the Mainland market. CEPA benefits Mainland enterprises by allowing Hong Kong to serve as a perfect “springboard” for them to reach out to the global market, accelerating the Mainland market’s integration with the world economy. By using this opportunity to establish businesses in Hong Kong, foreign investors can also capitalise on the CEPA benefits and join with local businesses in tapping the vast opportunities of the Mainland market. In accordance with Article 3 of CEPA, both the Mainland and Hong Kong will broaden and enrich the content of the arrangement through continuous and further reciprocal liberalisation. As of January 2012, the two sides had signed eight Supplements to CEPA, providing a total of 32 services liberalisation and trade and investment facilitation measures, which include...