

Joseph Yam: Mortgage-backed securities programme in Hong Kong

Speech by Mr Joseph Yam, Chief Executive of the Hong Kong Monetary Authority, at the signing ceremony of the Bauhinia MBS Programme of the Hong Kong Mortgage Corporation Limited, Hong Kong, 30 October 2003.

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Ladies and gentlemen, let me first offer a very warm welcome to all of you to this signing ceremony to mark the successful conclusion of the second series of mortgage-backed securities issued under the Bauhinia MBS Programme of the Hong Kong Mortgage Corporation. The issue size this time is HK\$3 billion. It is the largest residential MBS issue in Hong Kong, so far.

Ladies and gentlemen, as you are aware, the HKMC is committed to developing a deep and liquid MBS market in Hong Kong as an effective means for enhancing the availability of competitive mortgage finance in Hong Kong for homebuyers. The success of this initiative will also benefit both the financial market and the future development of the HKMC as a major financial institution.

For the financial market, MBS provide an efficient channel for long-term funds from the capital market to supplement bank financing of long-term mortgage loans. They also help banks to better manage the liquidity and maturity mismatch risks inherent in their mortgage business. Development of an active MBS market will broaden the product range of the financial market and further develop Hong Kong's role as an international financial centre.

For the HKMC, MBS provide an important source of funding and an effective tool for managing the risks of its fast-expanding mortgage portfolio. In a short span of six years, the Corporation's mortgage pool has increased to over HK\$32 billion, which is funded by debts of a similar amount. Momentum is expected to pick up further with the planned acquisition of between HK\$16 billion and HK\$20 billion of mortgage portfolios before the end of 2004. The proceeds from issuance of MBS help relieve the funding pressure of the mortgage purchase programme. The securitisation process also enables the Corporation to reduce the Prime-HIBOR basis risk and the refinancing risk of its mortgage portfolio.

There are in fact two MBS programmes that have been developed by the HKMC. We made a modest start in October 1999 with the launch of the Guaranteed Mortgage-Backed Pass-Through Securitisation Programme. There were a total of eight series of MBS issued under that Programme, with an aggregate amount of about HK\$2.8 billion. The back-to-back structure of the MBS issued allows the participating banks to keep a substantial portion of the cash flow from the mortgage pools, while reducing the credit risk and capital cost through the HKMC's guarantee of the securities. It also provides them with the option at any time to off-load part or all of an issue to suit their liquidity or trading objectives.

Meanwhile, it became clear to us that the standardisation of mortgage origination documents would facilitate the securitisation of mortgages more efficiently, by removing the need for due diligence review of documentation by credit rating agencies and investors. The HKMC therefore spent considerable efforts in promoting such standardisation. With the generous support of the legal fraternity and the banking industry, the HKMC introduced, in July 2001, the Model Mortgage Deed and the Model Deed of Guarantee and Indemnity. Fourteen major mortgage lenders have since adopted these model documents. Further standardisation of mortgage origination documents is in progress.

It was against this background that the HKMC found it able to embark on another MBS programme - the Bauhinia MBS Programme. The first series of MBS under that programme was issued in March 2002 and amounted to HK\$2 billion. The paper issued was in the form of bonds that investors are familiar, with a secondary market of considerable liquidity. Great care has been taken to design the Programme in such a way as to provide a convenient, flexible and cost-efficient platform for the issue of MBS. Benefiting from the standardisation of product structure and legal documentation, the lead-time for arranging an issue has been shortened substantially, from six to nine months for a stand-alone issue, to a few weeks under the Bauhinia MBS Programme.

The current issue of HK\$3 billion of MBS is the second series under the Bauhinia MBS Programme. We are grateful and greatly encouraged by the enthusiastic response of the underwriting banks and investors. The amount of HK\$3 billion has been fully subscribed by a diversified group of investors. They include not only banks, but also institutional investors and fund managers. The participation of these latter groups is especially welcome as a sign of the potential breath of the investor base for good

quality Hong Kong dollar debt securities. The opportunity has been taken to offer more choices to investors. These are explained in the technical note attached to the press release. The CEO of HKMC will be happy to explain these to you and answer any questions that you may have, later in the press briefing.

What I would like to do here in conclusion is to thank HSBC, the Lead Manager of this MBS issue for marketing it so effectively. I would also like to thank the Senior Co-lead Managers, Bank of China, Bank of Communications, Bank of East Asia, International Bank of Asia, Mitsubishi Securities (HK) and Co-lead Manager, BNP Paribas for their staunch support. The HKMC team has enjoyed working with all of you towards this successful result, and we look forward to your continuing active participation in future HKMC issues.

Thank you.