

## **Anselmo L S Teng: Financial innovation and the win-win outcome for the regional economy**

Speech by Mr Anselmo L S Teng, Chairman of the Monetary Authority of Macao, at the Pan Pearl River Delta Regional Cooperation and Development Financial Forum, in Chang Sha, Hunan Province, 9 June 2007.

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Honourable officials,  
Dear representatives,  
Ladies & gentlemen,

I am pleased to have the opportunity to participate in today's forum. On behalf of the Monetary Authority of Macao, I would like to share with you some viewpoints on the theme – “Financial Innovation and the Win-Win Outcome for the Regional Economy.” On this occasion, I would like to thank the elaborate planning and assiduous efforts displayed by the financial academies from nine provinces in organizing this forum and the meticulous arrangement made by the organizers and co-organizers. Here, I sincerely wish this forum a great success in materializing the objective of a win-win outcome for the region.

First, I would like to update you on Macao's economic and financial status. Then, I will share with you some of my views on the main theme.

As it is commonly known, the Macao Special Administrative Region is small with a rather limited economic capacity. Nevertheless, since the return to the Motherland, the Macao SAR is capable of achieving rapid economic growth with record achievement noted in the financial sector. This favourable result is attributed to the auspices of the Central Government and the fraternity of the provinces, cities and regions. In the first quarter of 2007, we achieved a real GDP growth of 25.6%, after having attained 16.6% in 2006. Rapid growth in foreign direct investment, private consumption and tourism services were the main propellers for the economic performance. Besides, we witness that the policies and measures diligently pursued by the MSAR government for proper economic diversification is taking shape. Apart from gaming, other forms of tourism such as corporate travel, culture and leisure, sports, convention and exhibition have been growing briskly. Meanwhile, change is also observed in the source of inbound tourists. Traditionally, China, Hong Kong and Chinese Taiwan are the major source of inbound tourists. Today, tourists coming from East Asia, Europe, the U.S.A., Japan, Korea and Australia have been growing at a faster pace. Other business sectors, including the financial sector, also enjoy better growth opportunities in the face of substantial gains recorded in overall consumption as well as local and foreign investments.

The local financial sector accounts for around 10% of GDP. It mainly consists of 27 banks and 25 insurance companies, which are mostly subsidiaries or branches of banks and insurance companies outside Macao. It is recognized as a pillar industry in terms of its total assets or its contribution to GDP. Buoyed by rapid local economic growth and sustained development in the neighbouring economies, the banking sector managed to achieve record performances year after year. As at the end of the first quarter of 2007, total assets of the banking sector grew by 22.3% year-on-year to MOP281.1 billion; deposits increased by 18.2% to MOP236.4 billion; loans reached MOP78.1 billion, representing an increase of 18.1%. Non-performing loan ratio was at record low of 1.1%. The overall profit for the first quarter jumped by 30.3% to MOP1.09 billion, after a notable result of MOP3.9 billion scored for the full year of 2006. Consolidated capital adequacy ratio of the whole sector at the end of 2006 was kept at a high level of 14.7%, well above the minimum 8% required by the Basel Committee. The favourable performance has not only reflected the result of the fast growth of the local economy and sustained development of the neighbouring economies, it is also the result of the unrelenting effort of the banking sector devoted to enhancing its risk management and financial innovation.

Financial innovation is a perpetual endeavour for the financial industry which covers a broad and wide-ranging scope. I consider that it should embrace new financial ideas as well as improving existing ones; in general, it covers the following 4 aspects:

1. Innovation in 3 main financial structures: financial market, financial institutions and financial products;

2. Innovation in 3 main financial channels: public financial infrastructures, internal operational facilities and external services measures;
3. Innovation in 3 main users of the financial system: government, enterprises and residents;
4. Innovation in 3 main financial regimes: financial rules and regulations, financial supervision and cross-border financial cooperation.

If the above definition of financial innovation is established, its realization will vary in accordance with time, place and people involved.

It would be unrealistic for Macao to realize an overall financial innovation. Macao's development is confined by many objective factors such as limited capacity, absence of a comprehensive financial market and lopsided economic structure. As such, our financial innovation effort is restrained by inherent factors. Nevertheless, all along, we have been actively promoting financial innovation in line with the needs of economic development which can simultaneously maintain the sustainable development of the financial industry in a stable and sound manner.

Being an operator, the local financial sector has been remarkable in financial innovation. In the past few years, we have witnessed the emergence of various types of financial products, ranging from telephone banking, mobile banking, online banking, investment fund, bankassurance, personal banking, private banking to privileged banking services.

Being a regulator, we allow adequate freedom to financial enterprises by adopting appropriate measures to innovate our system. To cope with actual market environment, we revise or relax enforcement of certain regulatory requirements subject to the premise that there is a thorough understanding of risk management capability of the sector. Furthermore, we continue to enhance our regulatory practice by conducting onsite investigation for a specific purpose. We gather thorough knowledge of a certain facet within a relatively short time span. Upon completion of the investigation, we share mutual findings with the inspected institutions in a timely manner with minimum disruptions to their daily operation while they all stand to benefit.

Being a facilitator, we organize activities for the industry participants to cultivate business opportunities locally and overseas through cross-border exchange and cooperation via various channels, especially liaisons with our regulatory counterparts and arrangements with other governments.

In comparison, the Mainland market is boundless. The government is easing control on financial regulations as reform of the financial system is moving forward on all fronts. The pattern of economic development and household consumption is changing while the Mainland economy continues to grow rapidly. Regional and global economic integration is gathering steam. Development in the securities market and the pervasiveness of renminbi carries profound implications. The combined effect of all these forces has not only contributed to the establishment of a solid and sound foundation conducive to financial innovation, it has also brought creative opportunities for financial innovation to the regions that are closely connected with the economic and financial development of the Mainland.

The PAN-Pearl Delta Region, 9 provinces and 2 special administrative regions are vast in area, each has its own competitive edge and solid economic strength. Their governments, business sectors and residents have comparatively better knowledge about finance. Against this backdrop, there is a great future for financial innovation. Although I have mentioned earlier that Macao has limited experience in this respect, I would like to take this occasion to share with you the following observations:

1. Appropriate laws and regulations are needed to foster a regulatory environment that is conducive to financial innovation. It is worthwhile to attempt new ideas as long as they would not contravene the requirements of existing laws and regulations. However, we must have a full understanding of the related risks. And, we must have an appropriate risk control system or measures to mitigate or eliminate the risks. Apart from complying with necessary regulatory procedure, the new ideas must facilitate market development without impairing the rights of consumers. To this end, the QDII scheme for stock investment can serve as a classic example. The introduction and moderation of the QDII scheme as well as the gradual opening of the Mainland capital market represent an important step towards financial system reformation. These measures are also financial innovation conducive to financial market development. Based on this situation, we can expect more innovation in financial policies. In the near future, a wave of keenly anticipated innovations in financial institutions, products, service and cooperation will arise from innovated financial policies.

2. There should be ongoing observation of changes in market development, analysis of special needs of customers, segmentation of customers and markets, as well as the establishment of a system to trace the demand of market and customers. The regulators should proceed in tandem with the pace of market development and monitor changes and characteristics of consumer demands. As far as financial products are concerned, asset management and structural financing that are selling like hot cakes are good examples.
3. Financial innovation should be adapted to time, place and people. This issue has been explored before with Macao as an example.
4. Maintain good communication between regulators and market participants. It is normal for regulators to receive tons of complaints and enquiries from consumers. As these letters are mostly pinpointing financial products and services, regulators would gain a better understanding or come up with a general idea on the types of services demanded by consumers during the course of handling these complaints and enquiries.
5. Investors and consumers need education. It is desirable to initiate a two-pronged measure. Based on the objectives of protecting the rights of the consumers and investors as well as facilitating the penetration of the financial market, the regulator can actively embark on financial consumption related education through various channels such as the media and topical exhibitions etc. On the other hand, the market participants are encouraged to launch more promotions that are infused with educational elements. This approach allows the participants to exploit potential business opportunities while fulfilling certain social responsibilities.
6. Cross-border exchange and cooperation are imperative. Apart from taking into full consideration the elements of time, place and people, we can benefit from observing the achievement of others in financial innovation. For products or services that are sophisticated or distinctive, we can study the concepts, repackage or adapt them for introduction to the local market. Much can be gained and shared from getting to know other markets through cross-border exchange. Through mutual understanding and interaction, we have better understanding of other markets and hence better knowledge. Since the return to the Motherland and the signing of the Closer Economic Partnership Agreement (CEPA), economic ties between Hong Kong, Macao and the Mainland have much strengthened. There will be profound implications if trade transactions between these places can be settled in Renminbi. This is a form of financial innovation which can only be materialized through cross-border cooperation involving not only the trading of commodities but also cooperation between the governments concerned. Now, I would like to share with you another live experience. As we all know, since the return to the Motherland, the Macao SAR government has been trying to turn Macao into a service platform for the Mainland and Portuguese-speaking countries by capitalizing on the historical relationship that Macao built up with the latter. Financial cooperation between Portuguese-speaking countries and MSAR has flourished from mere acquaintance. In September 2006, the Bank of China (Macao Branch), BPI of Portugal and its Angolan subsidiary, BFA, signed a tri-partite cooperation agreement in the annual "Macao International Trade & Investment Fair" ("MIF"). This agreement covers financial services including remittance made available to Chinese enterprises and workers in Angola. This appears to be a very simple cooperation arrangement. However, a closer look shows a few special features. Traditionally, similar arrangements involve only two parties. Now, this one involves one more party for a specific reason. The arrangement is not concluded for business between Macao and Angola or between Macao and Portugal. It is specially arranged for transactions between Angola and the Mainland. From this example, there is great potential for financial innovation in the area of cross-border cooperation. Besides, we believe that much can be achieved between the Pan-Pearl Delta Region and its brother provinces and regions, between Macao and the Mainland, as well as between the Mainland and Portuguese-speaking countries through Macao as the intermediary

The above is a summary of my basic viewpoints on the theme of this forum. It provides merely food for thought which I hope can lead to further elaboration from the audience.

Thank you!