

Peter Pang: Pilot platform for cross-border investment and settlement of debt securities

Remarks by Mr Peter Pang, Deputy Chief Executive of the Hong Kong Monetary, at the Press Conference on Pilot Platform for Cross-border Investment and Settlement of Debt Securities – Hong Kong, Malaysia and Euroclear Bank, Hong Kong, 13 March 2012.

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Deputy Governor Muhammad Ibrahim, Mr Anso Thiré, ladies and gentlemen,

Good afternoon. Let me welcome you all to this press conference to announce the launch of the strategic alliance of the cross-border bond investment and settlement platforms in Hong Kong, Malaysia and Euroclear Bank.

The Pilot Platform to be launched on 30 March under this strategic alliance goes well beyond commercial cooperation amongst the partners. It will advance the important policy objectives of fostering bond market development and promoting financial stability at both global and regional levels.

There are strong demand and supply side factors that focus global investors' attention on bond markets in Asia. On the demand side, the European sovereign debt problems and successive downgrades of sovereign credit ratings of the advanced economies underscore the need for geographical diversification by global investors. Asia is the obvious choice as it stands out as the bright spot and engine for global growth. According to IMF's forecast, emerging Asia, with China as the core, will contribute about 57% of the world's GDP growth by 2016. Augmenting this favourable demand factor is the improved credit ratings of Asian sovereign issuers. There are now 14 Asian economies at investment grades, of which, nine are at or above the single A rating.

At the same time, the supply side factors are also highly favourable. The huge financing needs of Asia will support a continuous expansion in bond issuance. According to the Asian Development Bank, Asia's infrastructure financing needs alone amounted to USD 8 trillion from 2010 to 2020. Equally important is the emergence of new and attractive bond asset classes. The two products that have caught most attention of global investors are the sukuk in Malaysia and the RMB dim sum bonds in Hong Kong. This is rightly so as these products connect the global market with the vast and increasingly prominent financial systems in the Islamic world and China.

We have seen very encouraging development of the sukuk market in Malaysia, the symbol of Islamic financing. The amount of outstanding sukuk in Malaysia increased substantially from MYR 146 billion (USD 41.3 billion equivalent) at the end of 2006 to MYR 361 billion (USD 113.9 billion equivalent) at the end of 2011. Meanwhile, the growth of the RMB debt securities market has been phenomenal. In a short space of 5 years, the annual issuance amount lodged with the Central Money Markets Unit (CMU) in Hong Kong increased by 16 times from a modest amount of RMB 10 billion (USD 1.4 billion equivalent) in 2007 to RMB 172 billion (USD 27.3 billion equivalent) in 2011. The growth momentum is expected to pick up further after China's announcement to formalise the use of RMB in foreign direct investment (FDI) in 2011. The upside is very significant as China's total FDI amounted to USD 116 billion in 2011, or RMB 750 billion equivalent.

Besides facilitating the rapid development of the sukuk and dim sum bond markets, more importantly, the Pilot Platform will contribute significantly to financial stability in the Asian region. With the advanced economies undergoing structural adjustment and fiscal consolidation, the two-speed recovery will continue to entice portfolio flows into Asia. The key challenges for Asia are to channel such flows to productive use, reduce concentration in short-term positions of the more volatile asset classes, and to avoid such flows spiking up a

property price bubble. Channelling the inflows into the bond market will serve these useful purposes as the investors are typically institutional investors who take long-term positions in strategic economic sectors.

The global financial crisis has reminded us of the destructive powers of a liquidity crunch and the need for quick access to local currency liquidity in times of stress. In particular, the increased risk aversion arising from the recent financial crises and heightened alertness to the counterparty exposure have raised the demand for secured lending. As an illustration, the average tripartite collateral management deals outstanding administered by Euroclear Bank increased substantially from EUR 76 billion in 2001 to EUR 325 billion in 2011. An important function of the Pilot Platform is to enable financial institutions to make use of securities held in one of the partner systems as collateral to conduct secured borrowing in the local currency of another partner economy. As an example, a European bank can make use of its securities held with Euroclear Bank as collateral to borrow Hong Kong dollar to meet the liquidity needs of its Hong Kong subsidiary. The cross-border and cross-currency collateral management service to be provided by the Pilot Platform is a timely solution to meet this market need, and will be a powerful tool to enhance financial stability in the partner economies.

Talking about the alliance we have, we are indeed very fortunate to have three strong institutions to be the founding partners of the Pilot Platform – the RENTAS in Malaysia, the CMU in Hong Kong, and the Euroclear Bank. Each will bring unique and valuable contribution to the partnership and the potential synergy would be substantial. Through RENTAS, global investors will have convenient access to Islamic bonds. In the other direction, Euroclear Bank's clients will benefit from the large and increasingly wealthy investor base in Southeast Asia and the Islamic world. Likewise, the CMU will provide an easy access to RMB bonds and highly rated bonds in other currencies for the global investors and enrich Euroclear's investor base with the fast expanding investor clusters in greater China. Euroclear Bank, with over 300,000 securities in 2011 and holds clients' assets valued at EUR 10.8 trillion, provides a huge reservoir to support cross-border cross-currency collateralised lending. Its large investor base will also provide a powerful platform for global investors to access the markets in Hong Kong and Malaysia. I would like to take this opportunity to thank Bank Negara Malaysia and Euroclear for sharing our vision and working with us to bring it to fruition.

The platform will offer a wide range of services to global and domestic investors. These services include a global securities database containing information of international and domestic securities, provision of a single point of entry to allow investors to buy and hold international and domestic bonds through their accounts of the local system, cross-border issuance and settlement of bonds in foreign currencies on a delivery-versus-payment basis, provision of an effective and efficient channel for cross-border cross-currency collateralised lending and borrowing between financial institutions, and automation and standardisation of the corporate action processing such as interest payments and redemption, distribution of corporate action notices, and exercise of custody instructions. My colleague Esmond will explain these arrangements in greater details shortly.

Finally, I would like to stress that the Pilot Platform to be launched is meant to be inclusive, not exclusive, and we welcome the participation of more parties. The benefits in promoting bond market development and financial stability can only increase with more bond investment and settlement systems in the region joining as partners. We will continue to work closely with Bank Negara Malaysia and Euroclear Bank to promote the platform to other central banks and securities settlement systems in the region and to implement additional services to the platform to meet evolving market needs.

Thank you.