Norman T L Chan: The importance of soft power in international financial centre

Opening keynote speech by Mr Norman T L Chan, Chief Executive of the Hong Kong Monetary Authority, at the Hong Kong Institute of Bankers (HKIB) Annual Banking Conference 2016, Hong Kong, 20 September 2016.

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Dr Patrick Fung, Ms Carrie Leung, distinguished guests, ladies and gentlemen, good morning to all of you!

1. Each year, the Annual Conference of the Hong Kong Institute of Bankers (HKIB) focuses on the topics most relevant to the banking industry and its practitioners, and invites prominent speakers and experts in the relevant field to share with the audience their insights. I am very pleased that I am being given the opportunity to speak today at the Conference. Previously at the HKIB and many other banking conferences, I had talked about the importance of "soft power", which in my view is the most crucial attribute that differentiates an international financial centre (IFC) from the rest of the crowd. If you feel bored with the theme of "soft power" and think that I should talk about a different or more exciting subject today such as those suggested by the MC, then I am afraid you will be disappointed. I can well understand the frustrations that some of you may have, but I, after very careful consideration, feel duty bound to embark on the same subject again. Please allow me to explain.

2. It is my strong belief that what differentiates an international financial centre (IFC) from the rest of the aspiring financial centres is its superior "soft power". An IFC is not about how big your airport is, how tall your buildings are or how fast your internet is. The hard infrastructure is important but most financial centres have equally good hardware. An IFC, just like a world class brand in merchandise goods, is all about good quality and high reliability. An IFC must be able to provide high quality and trustworthy financial services to customers in the neighbourhood and beyond. I should say that Hong Kong has already developed into a world class brand for financial services. No matter which narratives you choose to subscribe on how Hong Kong has come this far in the past three decades to where we are now, it is far too easy for us to feel complacent and lose sight of what has made Hong Kong an enviable success story in the past. Other than a nice harbour, Hong Kong is not endowed with any natural resources. Apart from people, and that's you, we have virtually nothing. But "people" is exactly what it takes to build a brand for financial services. It is also "people" that can bring Hong Kong to the forefront in the new era in the next 10, 20 and 30 years.

3. Banking has always been evolving over time, but I have not seen such drastic changes in the banking scene across the board since the Global Financial Crisis in 2008. I just came back from Basel last week to attend a meeting of Heads of Central Bank Governors and Supervisors. Many highly technical but important reform measures concerning the international standards on capital and leverage were discussed. This is part of the long process for the governments and regulatory authorities to try to rein in the banking sector, having learnt from the very bitter lessons during the Global Financial Crisis. I am not trying to debate today whether these new international standards are justifiable or needed. The point I wish to make here is that all these new standards are highly complicated and require special training and expertise to come to grips with them. So banks have to hire, train and retrain people in order to fully understand and implement the rapidly changing regulatory standards and requirements.

4. Apart from the badly needed capability amongst banks in capital, liquidity and credit risk management, the demand for enhancement and upgrading in banking conduct has also increased phenomenally in the last few years. Banking conduct covers a wide spectrum of banking businesses and I would like to focus on just three areas today:

(a) wealth management;

(b) anti-money laundering and counter-terrorist financing (AML/CFT) controls; and

(c) Fintech.

5. I believe there is very little disagreement amongst the audience today that Hong Kong has a huge potential in capturing the wealth and asset management business in Asia. The demand for top quality private wealth management services arising from the rapid and sustainable growth of affluence on the Mainland is particularly promising. However, private wealth management requires special skill-set, not only in product development but also in customers interfacing. Of course product issuers need to possess the technical know-how on how best to design products that can effectively meet the changing needs of the customers. It is equally important that the relationship managers have the necessary technical competence to fully understand the products and be able to explain the key features and risks to their customers. However, technical competence in understanding the latest ranges of financial products is simply not good enough nowadays. This is because the society today demands a high standard from financial intermediaries: i.e. fair treatment of customers. This means that financial firms must not put their own interests above those of the customers. Financial firms are expected to take care of the interests of their customers, including but not limited to those related to product suitability and concentration. This is a simple principle but very hard to achieve. If the treat customers fairly requirement is not demanding enough, there is the additional challenge brought about by the recent trend to raise the global standards in combating money laundering and terrorist financing. As it is well known to all, there can be quite serious consequences for AML/CFT breaches and failures.

6. It is therefore not surprising to see that many international banks have now been engaging in the so-called “de-risking” exercises. While there might be legitimate reasons for doing this, we have seen some side effects detrimental to financial inclusion from this de-risking process. In a nut-shell, to seek to de-risk using a “one size fits all” approach across all jurisdictions for an international bank may be easier or tidier from the compliance angle, it does not take into account the very diverse risk profiles of customers in different countries and in different business segments. The HKMA’s regulatory approach for banks in Hong Kong is one that is “risk based”, which means the banks should differentiate the likely riskiness of the customers and apply proportionate measures for the Know-Your-Customer (KYC) and due diligence process in account opening for new customers and in information gathering for existing customers. As you may be aware, I issued a circular earlier this month to all banks in Hong Kong providing an elucidation on the HKMA’s supervisory stance and requiring banks to review their existing practices with a view to changing them if there are inconsistencies with our risk-based approach. What I hope to achieve in Hong Kong is a robust AML/CFT regime in which we comply with all the relevant international standards and yet provide a sufficiently customer-friendly environment so that bona fide businesses and ordinary citizens can have full access to basic banking services. This is a tall order because it requires the senior management of banks to pay much closer attention to how their compliance and control systems should be structured so as to strike the right balance between de-risking and financial inclusion. Even if there is an appropriate control system in place, it still requires adequate training for the branch managers and frontline staff to fully understand the requirements of the HKMA and of the bank, and be able to exercise the necessary judgement so that customers can be treated fairly, thereby avoiding undue bad customer experience.

7. Now a word on “Fintech”. I think there is general consensus amongst all of us here that technology has advanced so much in the past decade or two that it has drastically transformed the way in which banking and financial businesses can and should be conducted. It is hard for bank customers to contemplate how they would manage if the internet or digital interface becomes dysfunctional for a couple of days. It is even harder for bankers to contemplate how they can survive for a day or just several hours if their systems are down due to DDoS or whatever reasons. No doubt the cyber world offers the kind of convenience and speed in transactions that are simply unthinkable just ten years ago. Clearly all of us must try our best to make full use of technology in the provision of solutions for financial services. I am

pleased to note that Fintech is making important headways in recent years. The bad news is, however, the digital world is equally, if not more, risky as the physical world. So on the one hand bankers need to embrace new technology but on the other they must upgrade their capability in safeguarding cybersecurity.

8. This brings me back to the main theme of my talk: "soft power". How do we develop and maintain superior "soft power"? It is very simple: "people", '"people" and "people". Without "people", Hong Kong has nothing. However, as competition from our neighbouring centres intensifies over the years, it is not only just "people' that we need. It's about how to turn "people" into "good people" and from "good people" to "great people". In this regard, there is an ancient Chinese idiom that says: "it takes 10 years to grow trees but 100 years to develop people" "十年樹木，百年樹人". When it comes to people, there are no shortcuts and there are no quick fixes. We fully understand this point and that is why the HKMA, in collaboration with HKIB, has been working very hard in the past few years to develop new competency enhancing training programmes for the banking practitioners. In June 2014, we rolled out the Enhanced Competence Framework (ECF) for private wealth management. I am glad to report that the programme has made very good progress with more than 1,600 private banking practitioners having achieved the relevant ECF benchmark so far. Today I am very pleased to announce that the HKMA will launch another ECF programme, which is designed for AML/CFT functions. The programme will be rolled out in three months' time in December. This is a Core Level module for new entrants in the field of AML/CFT. A more advanced level for practitioners with at least 3 years of relevant experience will be launched in June 2017. This new ECF should go a long way in helping enlarge the pool of qualified AML/CFT professionals, who are in short supply at the moment.

9. On Fintech, I announced in May this year that the HKMA would launch a "Cybersecurity Fortification Initiative". A core part of this Initiative is the rolling out of an ECF on cybersecurity so as to enlarge the pool of talents in this increasingly important field of banking. We are making good progress and I am pleased to announce that the Cybersecurity ECF will also be launched in December this year.

10. On a related note, I am pleased to know that HKIB is going to launch a new professional qualification, The Certified Banker (CB). Ms Carrie Leung, CEO of HKIB, will announce more details on CB in a moment. The curriculum of CB encompasses programmes under HKMA's ECF and combines the up-to-date industry knowledge, practical learning and professional competencies that are relevant to the banking environment.

11. Ladies and gentlemen, I make no apologies if you consider my talk on "people" development boring. As a result of the rising complexity of the financial industry, advance in technology and rapid change in the regulatory landscape, it is not possible for a banker to claim "I know it all"! It is only through continuous training and updating that a practitioner would be able to keep abreast of the latest developments in terms of technical knowledge and understanding of conduct and ethics requirements. While the HKMA will do whatever it can in promoting soft power upgrading, we can't do it alone. We must work together with the industry bodies, such as the Hong Kong Association of Banks, HKIB, the Treasury Markets Association, and the Private Wealth Management Association so that we can have common ownership of mission. It is also with the support and facilitation by the financial firms, as employers, that we can have full and active participation by banking practitioners in these training and talent development programmes. While there are costs and efforts in the short run, I am sure that over time they will bear handsome and profitable returns for the industry and practitioners alike.

12. In closing, I would say that the upgrading of our people from "good" to "great" is an uphill and ongoing campaign. We are still at the stage of promoting awareness and joint ownership of the mission amongst the industry and practitioners. We have also made good progress in developing the relevant training programmes for this purpose. Our supervisory

requirement at this stage is to encourage banks and practitioners to enrol into the relevant membership and take part in the training programmes. At the next stage when the infrastructure is more mature, the HKMA expects that banking businesses should normally be conducted by practitioners who possess the necessary technical competence and relevant qualifications in the areas concerned. Having said that, let me clarify one point. I am not presently envisaging a need for a mandatory qualification or licensing regime for banking practitioners, as such regime may not be flexible enough to cater for a fast expanding and changing banking business environment. All we need is for the official and private sectors to collaborate diligently in the joint mission of talent building. If we can get it right, which I am confident that we would, there is no doubt that Hong Kong will be able to succeed in maintaining Hong Kong's competitive edge as a world class brand for financial services. Thank you very much.