

**Technology, Change and Reform**  
*Implications for Hong Kong's Securities  
and Futures Markets*

**Indian Businessmen's Association**  
Luncheon

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**SFC**

證監會

# The Age of Technology

- ◆ If cars decline in price at the same rate as the price of PC computing power, the price of a car would be US\$5
- ◆ Internet financial transactions cost one US cent each - paper-based transactions cost US\$1
- ◆ E-trading did not exist before 1995 - 10 mn investors can now choose from over 100 online brokers in US alone. Online trading accounts for 25% of all trades on NYSE and Nasdaq

# The future of E-trade

- ◆ E-Schwab opened 1.4 million new accounts in 1998. Charles Schwab market cap now US\$41.5 bn - size of the Thai market and bigger than Boeing or Merrill
- ◆ Amazon.com market cap just under the Jakarta market cap
- ◆ 8 traditional SEC registered stock exchanges, vs more than 20 electronic trading systems

# Only the paranoiacs survive

- ◆ **Technology brings**
  - **change**
  - **confusion**
  - **competition**
  - **consolidation**
- ◆ **Cuts out the traditional middle-man**
- ◆ **But offers creativity and opportunity**

# Competition and consolidation of exchanges

- ◆ Merger talks between London and Frankfurt
- ◆ Paris, Madrid and Milan on Pan-European exchange
- ◆ CME, MATIF and SIMEX alliance
- ◆ Listing of Stockholm, Amsterdam and Australian exchanges
- ◆ Plans for listing of Toronto, London, Athens and Singapore exchanges

# Maintaining the Status Quo is not an Option

- ◆ Globalisation of the international financial markets
- ◆ Advances in information technology
- ◆ Increasing sophistication of investors
- ◆ New challenges brought to the local securities and futures market
- ◆ Hong Kong has to increase its competitiveness to rank among the world's most advanced and sophisticated financial centres

# Three-Prong Reform Programme for Securities and Futures Market

- ◆ **Upgrading of financial market infrastructure**
  - setting up of the Steering Committee on the Enhancement of Financial Infrastructure
- ◆ **Regulatory reform**
  - Composite Securities and Futures Bill by year end
- ◆ **Demutualisation and merger of the Exchanges and Clearing Houses**

# Upgrading of the Infrastructure of the Financial Market

- ◆ RTGS in December 1996 brought one-leg of infrastructure improvement
- ◆ DvP and PvP possible, but not yet in Securities area
- ◆ We have 3 separate trading and clearing systems that are not linked to each other
- ◆ Opportunity to effect STP [straight thru processing] and cross margining efficiencies
- ◆ Unified clearing also improves overall risk management

# Upgrading of the Infrastructure of the Financial Market

## Steering Committee on the Enhancement of Financial Infrastructure (SCEFI)

- ◆ Chaired by SFC Chairman
- ◆ Representatives from Exchanges, Clearing Houses, government and the Hong Kong Information Technology Association
- ◆ Met already 5 times
- ◆ Recommendations to FS in six months

# Upgrading of the Infrastructure of the Financial Market

## Terms of reference:

- ◆ Single clearing arrangement for securities, stock options and futures;
- ◆ Enhancement of the financial technology architecture to facilitate straight through processing
- ◆ Introduction of open, secure, scripless market, fully up to G-30 standards

# Regulatory Reform

- ◆ **Update to best international standards**
  - **to provide sufficient protection to investors**
  - **to be technology and innovation friendly**
  - **to be disclosure based regulation**

# Regulatory Reform

## Composite Securities and Futures Bill

- ◆ Clarification of regulatory objectives of SFC
- ◆ Strengthened supervisory and investigative powers
- ◆ Civil fine based enforcement
- ◆ Market Misconduct Tribunal
- ◆ New regulation on internet trading
- ◆ A streamlined licensing regime for market intermediaries

Bill to be introduced into LegCo by end of 1999

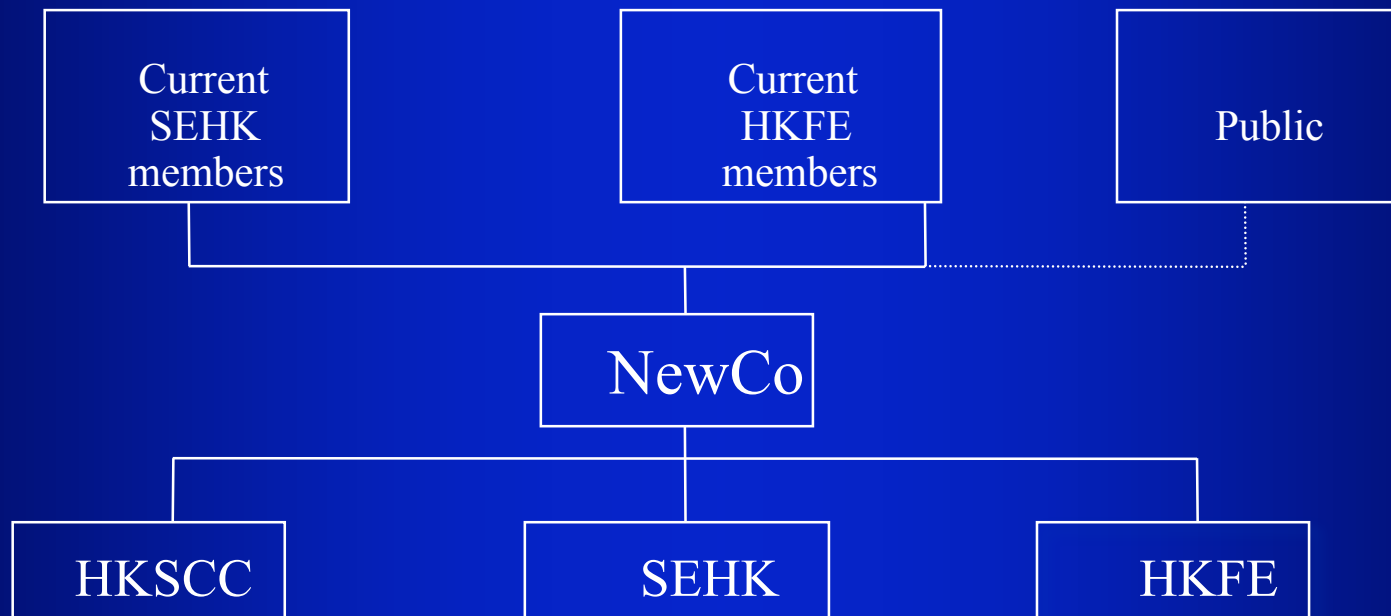
# Demutualisation and Merger

## 8 clear benefits

- ◆ Separation of ownership & trading rights - no reduction in rights
- ◆ New flagship blue chip financial company
- ◆ Economies of scale & operational efficiency
- ◆ Exchanges & clearing house response to market and competitive forces
- ◆ Greater range of services, eg information, GEM, back-office services for smaller brokers
- ◆ Raise new funds through listing to invest in technology
- ◆ Streamlined regulatory functions
- ◆ Devote energies to face external competition

# Demutualisation and Merger of the Exchanges and Clearing Houses Organisation Chart

- ◆ Demutualise, merge and list the exchanges and clearing houses under new holding company (NewCo):



# Demutualisation and Merger of the Exchanges and Clearing Houses

## Key features

NewCo - subject to profit making objectives

Board representation from all interested bodies  
(brokers, investors, issuers, Government)

Former members can sell ownership rights while  
still maintaining trading rights

Independence of NewCo protected by limits on  
shareholding

# Demutualisation and Merger of the Exchanges and Clearing Houses Follow Commercial Process

- ◆ two parallel and inter-conditional schemes of arrangement (one for SEHK and one for HKFE)
- ◆ the schemes will follow Companies Ordinance procedures

# Demutualisation: Working Groups

- ◆ Formation of sub-groups to rationalise the following regulatory functions
  - market surveillance
  - users regulation
  - listing/corporate finance
  - compensation arrangements
- ◆ Supported by financial, operational, legal and accounting advisers

# Demutualisation and Merger of the Exchanges and Clearing Houses

## Time is of Essence

### Timetable:

- ◆ **Mid-June 1999 - valuation and initial agreement on terms and conditions for merger ready and made public**
- ◆ **End July 1999 - scheme documents issued to members of the two Exchanges**
- ◆ **Mid-August 1999 - Members' general meeting of two Exchanges**
- ◆ **End September 1999 - Court sanction**

## Time is of Essence

- ◆ **By 30 September 1999, all non-legislative steps must be completed**
- ◆ **Legislative process by March 2000**
- ◆ **Listing of NewCo by 30 September 2000**

# Wired global marketplace - who will win? *Jeff Papows, CEO, Lotus*

- ◆ Which [economy] will develop inexpensive, high-bandwidth systems?
- ◆ Which [economy] will provide or enable nearly universal citizen access?
- ◆ Which [economy] will do the best job of updating existing bodies of law to accommodate new technological capabilities?
- ◆ Which [economy] will have the most capable, creative, and enthusiastic citizens and entrepreneurs?