Speech by SFST at 18th Hong Kong Venture Capital and Private Equity Association China Private Equity Summit (English only)

Following is the speech by the Secretary for Financial Services and the Treasury, Mr James Lau, at the 18th Hong Kong Venture Capital and Private Equity Association (HKVCA) China Private Equity Summit today (May 30):

Conrad (Co-chairman of HKVCA PRC Committee, Mr Conrad Tsang), Rebecca (Co-chairman of HKVCA PRC Committee, Ms Rebecca Xu) distinguished guests, ladies and gentlemen:

Good morning. I am delighted to join you at today's HKVCA Summit. From your agenda, I see a lot of experts will be speaking about China investment opportunities in a good range of areas. There is also a session this morning on the US-China trade relations. Actually, a while back when I accepted the invitation to address you here, I thought there was a good probability that a deal would have been struck and the air would have cleared by the end of this month. But, alas, this has not been so. And the prospect seems to bob up and down, and the stakes are getting higher and higher.

By now, it seems pretty obvious that the US-China trade tension is going to be around for quite a while, and this will be a factor foremost on the minds of investors. So I would start this morning by sharing a few thoughts on the subject. I would then explain why, notwithstanding such tension, I still see many promising opportunities in China.

To begin with, it has been suggested that China, after joining the World Trade Organization (WTO) in 2001, has since had a free ride to become a major trading economy, and the second largest economy in the world.

Back in 1986 to 1990, I was based in Geneva doing the Uruguay Round of Multilateral Trade Negotiations. This was the eighth round of trade negotiations under the General Agreement on Tariffs and Trade (GATT), which got transformed into the World Trade Organization on January 1, 1995. Hong Kong, along with many GATT and WTO members, has been a staunch supporter of the multilateral trade framework – we decry protectionism and advocate free trade. GATT and WTO indeed have really fostered the development of international trade and helped many developing economies to move up the development ladder. These efforts were reinforced by the International Monetary Fund (IMF) and the World Bank, plus a host of other multilateral development banks established subsequently, the latest being the Asian Infrastructure Investment Bank spearheaded by China. All these institutions have helped to promote more broad-based development and growth, especially beneficial for the developing economies, and this has also given impetus to free trade and globalisation.

However, with the rise of populist and nationalist sentiments in recent years, the global economic system begins to see the resurgence of protectionist measures, moving away from multilateralism. The current US-China trade is a case in point. The US has in fact also announced measures targeting other trading partners but it seems that some of the measures have been put on hold while the US is focusing on the negotiations with China.

China has come a long way since its economic reforms begun 40 years ago. It is true China's economic growth has been consolidating and gone are the days of double digit GDP growth. Yet, if you take a look at China's economy today, it has held stable so far, thanks to its resilient fundamentals. Last year's growth was still at a respectable pace of 6.6 per cent. This is faster than most other major economies and China continues to contribute around one third of annual global growth.

In the first quarter this year, the Chinese economy grew at a better than expected pace of 6.4 per cent. The latest indicators also show that internal demand in China remained stable in the first four months of this year.

In anticipation of the likely slowdown, China has pledged to further strengthen countercyclical policy adjustments to ensure economic stability. These include an RMB2 trillion reduction in taxes and fees in 2019, measures to stimulate credit to private and small enterprises through targeted cuts in the reserve requirement ratio, and expansion of the issuance of special bonds by local governments to support infrastructure investment.

From a long-term perspective, China's shift to higher quality economic development through deepening reforms and further opening up will put it on a more balanced and sustainable growth path.

Having said that, the ongoing US-China trade tension without a doubt poses challenges for the economic outlook ahead. The IMF estimates that the additional impact of the recently announced and envisaged new US-China tariffs will subtract about 0.3 per cent of global GDP in the short term. Moreover, failure to resolve the trade differences could further dent business and financial market sentiments, and lower global productivity and welfare. At the risk of stating the obvious, the US-China trade tension affects not just China's trade and economic growth but also the US and many other economies due to the disruption of the global supply chain and the hike of domestic prices on account of the punitive tariffs, hurting domestic consumers.

As scholars have pointed out, the international order now faces the challenge brought about by changes in the geopolitical landscape. Last year, in light of the ongoing US-China trade tensions, the Financial Times chose "Thucydides' trap" as the term that would summarise 2018 in a word.

The term was coined in 2012 when Harvard professor Graham Allison said that, "The defining question about global order in the decades ahead will be: can China and the US escape "Thucydides' trap?" The trap refers to the conflict between an established power and a rising power.

As early as in 2013, President Xi Jinping told a group of visitors that, "We must all work together to avoid Thucydides' trap." President Xi has also emphasised that, "The notion that a great power is bound to seek hegemony doesn't apply to China, which lacks the gene that spawns such behaviour."

Just last month, President Xi reiterated China's commitment to reform and opening up at the Second Belt and Road Forum held in Beijing. First, China will expand market access for foreign investment. This includes all-round opening up of modern services, manufacturing and agriculture. China will also allow the operation of foreign-controlled or wholly foreign-owned businesses in more sectors, and accelerate the adoption of supporting regulations to ensure full implementation of the Foreign Investment Law.

Secondly, China will intensify efforts to enhance international co-operation in intellectual property protection, creating an enabling environment for innovation, and promoting technology exchanges with other countries on the basis of market principles and the rule of law.

Thirdly, China will work harder to ensure the implementation of opening-up related policies. China will overhaul and abolish unjustified regulations, subsidies and practices that impede fair competition and distort the market. China will also treat all enterprises and business entities equally, fostering a business environment based on market operation and governed by law.

For us in Hong Kong, we think that a trade war benefits no one, and we hope that the US and Mainland China will continue constructive talks and reach an amicable agreement soon. This will be for the benefit of not just the US and China, but the global economy as a whole.

Let me turn briefly to my second topic on the opportunities in China. The Greater Bay Area and the Belt and Road Initiative present opportunities for all countries. I am pleased to see eager and meaningful participation of many economies, large and small, in these two initiatives, which both originated in China. This is a testament to China's openness to the world and the commitment to collaboration with the international community.

For the Greater Bay Area, I noted a very high degree of interest among overseas businesses and investors during my duty visits to London, Dublin, Frankfurt and Zurich in the past year. For example, earlier this month, I visited London for the UK-Hong Kong Financial Services Government Dialogue and one of the key areas of discussion was the Greater Bay Area.

The Outcome Statement for this year's Dialogue stated that both Hong Kong and the UK recognised the opportunities for financial sector co-operation, liberalisation and opening up in the Greater Bay Area. In particular, Hong Kong can serve as a base to enable international investors and market participants to do business and invest in the Greater Bay Area while upholding international standards.

While a world-class financial services sector is a traditional strength of Hong Kong, we are also seeing amazing momentum in our ecosystem in innovation and technology. Here, I would like to highlight in particular our potential for healthcare technologies. In fact, of the two research clusters we are developing in the Hong Kong Science Park, one of them is in healthcare technologies.

Institut Pasteur from France and Harvard University from the United States have announced plans to set up research centres in Hong Kong for immunology and precision medicine respectively. This follows the Karolinska Institutet of Sweden, which opened its first overseas research facility in Hong Kong in 2016 to focus on stem cell biology, biomedical engineering and regenerative medicine.

Indeed, Hong Kong has a distinct advantage in advancing new medicines for the vast Chinese market. This is because clinical trials in three Hong Kong hospitals, namely Queen Mary Hospital, Prince of Wales Hospital and Hong Kong Eye Hospital, can be used to support the filing of new drug applications with the China National Drug Administration.

As for the Belt and Road initiative, we are pleased to note that Sir Douglas Flint, who served as Group Chairman of HSBC from 2010 to 2017, was appointed in December 2017 as Special Envoy to the Belt and Road Initiative of the British Treasury. Sir Douglas has identified three phases to improve UK-China co-operation for the Belt and Road Initiative.

The first phase was to set up an Expert Board to combine the best talents from China and Britain to clarify the financing standards that would build the most capacity. The second phase is to take the standards within a framework to build funds that can invest the money. The third phase is to build a network of suppliers and contractors who want to engage in international infrastructure projects.

Aside from the UK, Switzerland also signed a Memorandum of Understanding (MoU) with China in April this year to expand co-operation on trade, investment and finance for projects in third countries along the Belt and Road. Co-operation will be based on five key principles, namely, private capital for private projects, sustainable handling of debts, consideration of social impacts, environmental protection criteria, and transparency.

Importantly, the MoU contains a catalogue of basic principles for co-operation in line with international standards and legislation in the countries concerned, which are consistent with the UN Sustainable Development Goals.

Now this brings me to my final point on sustainable development. This is important to the discussion because this is an area in which China has assumed global leadership and welcomes international dialogue and co-operation despite ongoing trade tension.

You may know that China was the biggest investor in renewable energy globally in 2017, representing more than 45 per cent of total investments. China accounts for around 60 per cent of global solar cell production, and is number one in the world in terms of both the growth rate and existing stock of electric vehicles.

China has also emerged as a leader in green finance. In 2017, China's green bond issuance that aligned with international green bond definitions totalled around US$23.5 billion. The corresponding figure for 2018 was US$31.2 billion, around 18 per cent of the global market and second only to the US.

As for Hong Kong, we also have an important role as a regional hub for green finance. In 2018, around US$11 billion worth of green bonds was issued in Hong Kong. Issuers included entities from Hong Kong and Mainland China, as well as multilateral development banks such as the World Bank, the Asian Development Bank and the European Investment Bank. Last week, our Hong Kong Government issued US$1 billion worth of green bonds with a tenor of five years; this was three times over-subscribed and the accepted yield was 32.5 basis points over five-year US Treasuries. In the secondary market, the spread has tightened below 30 basis points.

We also seek to be a hub for thought leadership and international dialogue in green finance. In early 2020, the Hong Kong Monetary Authority and the International Finance Corporation (IFC) of the World Bank Group will co-organise the IFC's Sixth Annual Climate Business Forum in Hong Kong. The Forum will bring together global policymakers and finance leaders to share knowledge and expertise on growing climate business investment in emerging markets. I welcome all of you to take part in it.

Ladies and gentlemen, in conclusion, while I do not have a crystal ball to read the future for you, let me recapitulate the messages that I shared with you just now. First, it will be in everyone's interest for the world not to digress from the multilateral trading system. Secondly, the exciting initiatives of the Greater Bay Area and the Belt and Road present many opportunities for local and international investors. Thirdly, we see room for international dialogue and co-operation in promoting green and sustainable development. Let us do something for our next generations and leave a respectable legacy for them. I wish you all a successful conference. Thank you.