

Institutional and Structural Factors in Developing Chinese Securities Markets

Geng XIAO
Head of Research
Securities and Futures Commission
28 September 2001

1

Chinese Securities Markets (end July 2001, US\$ bn)

	<u>Mainland</u>			US	Japan	Taiwan
	HK	Mainland	& HK			
GDP (2000)	163	1,080	1,243	10,114	4,755	310
- ranking in the world	25	6	6	1	2	16
Market cap	547	561	1,108	14,337	2,752	207
- ranking in the world	10	9	6	1	2	14
Turnover*	272	588	860	26,062	1,777	577
Turnover* /Mkt cap(%)	50%	105%	78%	182%	65%	279%
Market cap / GDP (%)	336%	52%	89%	142%	58%	67%
Turnover* / GDP (%)	167%	54%	69%	258%	37%	186%
P/E ratio (times)	16	55	n.a.	26	73	14

US markets refer to NYSE and Nasdaq; P/E ratio is the weighted average.
*For the 12-months ending July 2001

2

Property Rights and Securities Markets

- ◆ **Delineation, protection and enforcement of property rights and contracts are critical to securities markets**
 - The value of securities depends on the quality of listed enterprises
 - The quality of listed enterprises depends on property rights and incentive structure
 - Property rights and incentive structure depend on legal and regulatory rules, corporate governance as well as social and cultural traditions
- ◆ **Institutional costs (transaction costs) and structural costs (factor costs) are all relevant in determining the competitiveness of securities markets**
 - Each market has its own strengths and weakness
 - Cooperation would reduce the total costs

3

Institutional and Structural Costs

	<u>HKSAR</u>	<u>Mainland</u>	<u>US</u>	<u>Taiwan</u>
Production Costs	High	Low	High	High
Transaction Costs	Low	High	Low	High
Strategic Planning Costs	High	Medium	Low	High
Sunken Social Costs	Low	High	Medium	Medium
Saving Rate	Medium	High	Low	High
Expected Investment Return	Low	High	Medium	Low
Product/Service Outflow	0	+	-	+
Capital Inflow	0	+	+	-
Exchange Rate Regime	Linked	Fixed?	Floating	Floating

4

Strengths of HKSAR

- ◆ **Low Transaction Costs**
 - Rule of law with advanced property rights system
 - Free and open economy with world-class financial system
 - Low tax rate and simple tax system
- ◆ **Stable Exchange Regime and Open Capital Market**
 - Fully convertible currency
 - Fully open capital market
 - Exchange rate linked firmly to USD
- ◆ **Next to Rapidly Growing Southern China**
 - Potential for lowering production costs in HKSAR
 - Potential for expanding turnovers in HKSAR
 - Potential for raising living standards in HKSAR

Challenges to HKSAR

- ◆ **Near term**
 - **Lower Factors: leverage resources in Shenzhen by selective loosening of economic border**
 - **Close Gaps with London/New York: better regulation, more products, higher turnovers**
 - **Build Links with Mainland: more research, better marketing, closer cooperation**
- ◆ **Medium and long-term**
 - **Integrate HKSAR/PRD economy**
 - **Wall Street in Asia**