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**Statement by Ms. Mannathoko and Mr. Garang on People's Republic of China - Hong Kong Special Administrative Region
(Preliminary)
Executive Board Meeting
May 21, 2021**

We thank staff for the comprehensive report, and Messrs. Jin and Law for their insightful Buff statement.

The authorities' policy prudence has ensured the resilience of the financial system in Hong Kong SAR with a well-structured macroprudential framework and sound policies and adequate buffers to cope with cyclical downturns and future shocks. The banking system remains well capitalized and the liquidity position remains robust. This notwithstanding, vulnerabilities relating to foreign bank branches, investment funds, households, and nonfinancial corporates require vigilance. The FSSA highlights areas where the main macro-financial risks originate, including stretched real estate valuations, and global risk premia, among others. In addition, the financial sector remains exposed to climate change risks. Close monitoring of the sector, alongside the development of comprehensive policies for green and sustainable finance is likely to be beneficial, and with this in mind, we are in broad agreement with staff's appraisal and recommendations.

We encourage the authorities to increase their attention to banks with foreign links.

Greater oversight over banks with both foreign branches and local subsidiaries in Hong Kong SAR will be essential to contain risks of significant spillovers from foreign branches to other financial sectors both at home and abroad. Similarly, closer monitoring of liquidity risk for banks operating with multiple group entities is needed to ensure that banks adhere to internal risk management practices.

Ensuring that nonbank mortgage lending is covered within the regulatory framework will also help to counter risks of a hidden escalation of vulnerabilities outside the purview of regulators, that could also spillover into the banking sector, given linkages between the bank and non-bank financial sectors. A strengthened framework for cross-sectoral resolution and

safety nets will also be beneficial. We welcome the authorities' intention to remain vigilant and to closely monitor real estate risks and act in a timely manner as needed, as described in the Buff statement. While household balance sheets remain strong, we nevertheless encourage continued close monitoring of rising household debt in the wake of the pandemic. The same also goes for the corporate sector. For crisis management and resolution, we applaud the comprehensive resolution regime adopted under the Financial Institutions Resolution Ordinance in 2017 which has strengthened crisis management arrangements significantly. Additional measures in this area are welcome.

A more proactive cross-sectoral approach could also be adopted to address risks posed by Fintech which pervades numerous activities. Coordinated efforts among regulators can also enable a more consistent and cross-sectoral approach, and support harmonized frameworks for cybersecurity-related reporting, information sharing, and monitoring the implications of artificial intelligence. We also note that Hong Kong SAR is well positioned to develop new fintech initiatives given its traditional strength in financial services.

Given the increasing complexity and interconnectedness of the financial system in Hong Kong SAR, stronger communication is becoming more important, and a comprehensive and dedicated semi-annual financial stability report will help. In addition, in light of its international standing and to preserve competitiveness, we encourage the authorities to continue strengthening the independence of the HKMA and fortifying its foundation for competitiveness in the financial sector.

We agree that climate risk should become part of systemic risk analysis and encourage the authorities in this regard. To this end, the authorities' plan to enhance mandatory disclosures, common taxonomies, and risk assessments is welcome and should help improve the pricing of climate risks. Given the need to develop green lending finance, and to monitor and manage the transition risks for the economy and financial sector, we encourage the authorities and staff to consider these issues in the next Article IV, to augment analysis of evolving macro-financial risks.

With these remarks, we wish the authorities success in their reform endeavors.