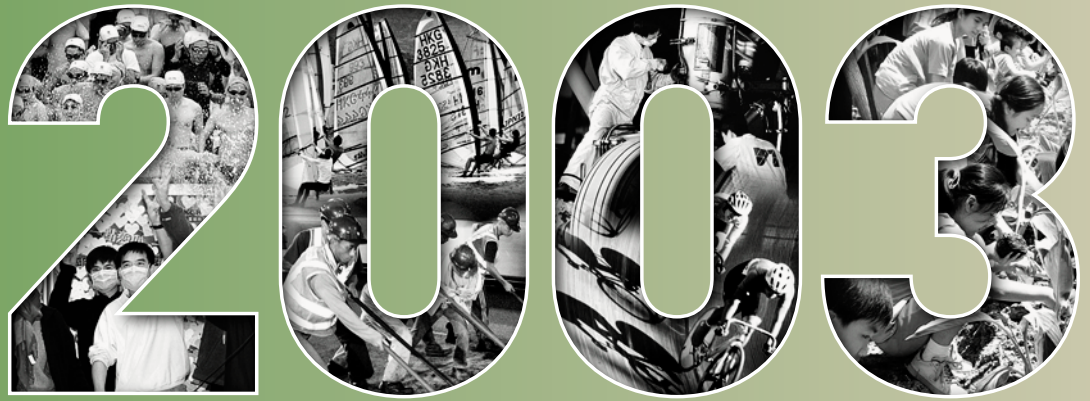


ANNUAL REPORT




HONG KONG MONETARY AUTHORITY
香港金融管理局

Contents

2	Highlights of 2003
4	Chief Executive's Statement
10	About The HKMA
14	Advisory Committees
20	Chief Executive's Committee
24	The HKMA: The First 10 Years
33	Economic and Banking Environment
51	Monetary Stability
57	Banking Stability
75	Market Infrastructure
83	International Financial Centre
87	Reserves Management
92	The Exchange Fund
123	Professional and Corporate Services
132	Calendar of Events 2003
134	Annex and Tables
157	Abbreviations used in this Report
158	Reference Resources

The chapter on Banking Stability in this Annual Report is the report on the working of the Banking Ordinance and the activities of the office of the Monetary Authority during 2003 submitted by the Monetary Authority to the Financial Secretary in accordance with Section 9 of the Banking Ordinance.

This Annual Report makes reference to documents and other materials available on the HKMA website www.hkma.gov.hk. These references appear as  > in the relevant parts of the Report, followed by navigation guidance from the HKMA homepage.

The full text of this Report is available on the HKMA website in interactive form and on PDF files.

A summary version of this Report is also available.

All amounts in this Report are in Hong Kong dollars unless otherwise stated.



Medical staff from the Prince of Wales Hospital meet the world on their discharge from hospital on 29 March 2003 after having recovered from SARS.

PROFESSIONAL AND CORPORATE SERVICES

In-house professional and corporate services enable the HKMA to fulfil its statutory obligations in maintaining monetary and banking stability in Hong Kong. Greater efficiency resulted in cost saving. Services were improved to keep pace with developments in banking and related activities, and advances in information technology. Other measures were implemented to make the HKMA more accessible to the public.

THE HKMA IN THE COMMUNITY

As the central banking institution in Hong Kong, the HKMA places great emphasis on promoting an understanding of its policies and work among the public. This policy of transparency and accessibility is realised through a number of channels:

- extensive contacts with the media
- regular and special publications
- a large and comprehensive bilingual website
- public access to the HKMA Information Centre
- an annual education programme for students and community groups
- frequent meetings with legislators
- a public enquiry service staffed nine hours a day.

These services are co-ordinated by the Corporate Development Division within the Corporate Services Department. The Division is responsible for providing media, publications and public relations services to the HKMA. It also supplies

translation and drafting services and secretarial support to the Exchange Fund Advisory Committee (EFAC) and its sub-committees.

Media relations

The news media play an essential role in the effective communication between the HKMA and the community. To promote transparency of its policies, the HKMA continued to maintain its ties with the print and electronic media in 2003.

Ten press conferences were held and 259 press releases were issued during the year. An average of 40 press enquiries was received by the HKMA every day. Educational briefings were arranged for reporters and editors on the topic of deflation.

The HKMA has strengthened the disclosure of information in its press announcements. For example, the disclosure of statistics relating to residential mortgage lending was improved through additional disclosure of the loans written off over the past 12 months, as well as the number of new loans approved in the primary, secondary and refinancing markets.

 [Information Centre > Press Releases](#)

Publications

The HKMA produces a variety of publications on monetary, banking and economic issues to provide information and data, and promote greater understanding of the work of the HKMA.

The *HKMA Annual Report 2002*, published together with its summary booklet and interactive website version, won the silver award in the Hong Kong Management Association's Best Annual Reports Award: the Report was commended for its comprehensiveness and good disclosure of corporate governance and future plans.

The *HKMA Quarterly Bulletin* and on-line *Monthly Statistical Bulletin* were redesigned with expanded content in early 2003. They continued to be a regular source of HKMA information, policy explanation and research findings. The *Quarterly Bulletin* included the HKMA's first *Half-Yearly Monetary and Financial Stability Report* in its December 2003 issue. The Report provides descriptions and analyses of external and domestic factors that have a bearing on Hong Kong's monetary and financial stability. It represents the HKMA's view of the main forces acting upon the Hong Kong economy, paying particular attention to the implications for the monetary and financial systems.



Selected HKMA publications published in 2003.

The second in a series of HKMA background briefs – *Banking Supervision in Hong Kong* – was published in March 2003. This booklet introduces and explains the main features of Hong Kong's banking system and the HKMA's supervisory approach. The HKMA also published information leaflets on security features for the new Hong Kong banknotes, safety procedures for Internet banking, and investor information on Exchange Fund Notes.

[Information Centre > Publications](#)

The HKMA on-line

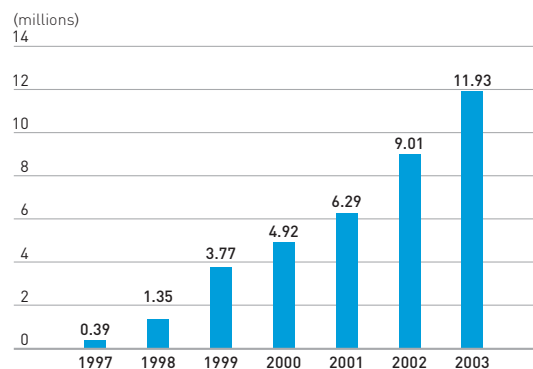
The HKMA website www.hkma.gov.hk is a comprehensive source of HKMA news and information instantly accessible to people throughout the world. In 2003, annual website page views reached almost 12 million (Chart 1), a 32% increase over 2002. Around 1,850 subscribers now receive the latest HKMA news through a daily e-mail news service.

In April, the HKMA website launched a new on-line public register containing specified particulars of the staff of authorized institutions engaged in securities business.

Information sections were launched during the year to introduce the newly opened HKMA Information Centre, new Hong Kong banknotes and investor information on Exchange Fund Notes.

[What's New > HKMA News Update E-Mail Service](#)

CHART 1 Page views of the HKMA website



Public education programme

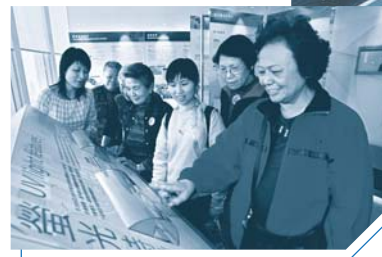
A permanent HKMA Information Centre was opened on the 55/F of Two International Finance Centre in December 2003. The Centre, which consists of an exhibition area and a library, introduces the work of the HKMA and houses over 20,000 books, journals and other texts on central banking and related subjects. The Centre is open to the public six days a week.

Using interactive presentations and video montage as well as the more traditional panels and material exhibits, the Centre's exhibition area displays the history of money and banking in Hong Kong and the key policy objectives of the HKMA. The exhibition area is divided into four main sections. A *currency section* traces the development of money and banking in Hong Kong and shows examples of coins and notes used over the years in and around Hong Kong. A *policy section* explains the work of the HKMA. A *topical section* focuses on issues of current interest. A *timeline*, outlining Hong Kong's monetary and banking history, runs along the whole length of the main wall of the exhibition area.

The library, situated just beyond the exhibition area, contains research materials for detailed study of Hong Kong's monetary, banking and financial affairs and of central banking topics elsewhere in the world. The main elements of the collection are



Visitors learn about monetary history and security features on new banknotes at the HKMA Information Centre.



publications by the HKMA, other central banks and international organisations, books and journals on monetary, banking, economics, finance and related subjects as well as an electronic register of authorized institutions in Hong Kong, maintained under section 20 of the Banking Ordinance. An on-line catalogue is available at the terminals inside the library and on the HKMA website.

Daily guided tours are organised for visitors and groups. In December, a total of 2,002 visitors and 21 schools, community groups and other organisations visited the Centre.

 [HKMA Information Centre](#)



The library



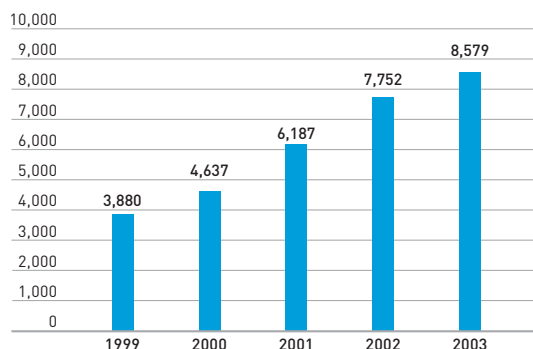
The exhibition area

The HKMA continued to organise its annual education programme for students, teachers and other groups. During the year, 15 seminars were organised for more than 4,000 students, teachers and members of various organisations. The Linked Exchange Rate system, monetary development in Hong Kong and the new banknotes were the main themes for the seminars. Since the launch of the education programme in 1998, more than 24,000 students and teachers have participated in the seminars.

Public enquiries

The number of public enquiries to the HKMA reached a record high in 2003. The HKMA received a total of 8,579 public enquiries during the year (Chart 2), representing an increase of 11% over 2002. These enquiries, which were received mainly by telephone, consisted for the most part of requests for statistical or background information on banking, monetary and HKMA-related issues from researchers, industry professionals, students and the general public: they also included complaints and suggestions. The HKMA is committed to delivering a speedy and informed response to all enquirers.

CHART 2 Total number of public enquiries



HUMAN RESOURCES

The Human Resources Division provides the human resources support and associated framework to facilitate the HKMA in meeting its policy objectives and day-to-day operations.

Organisational changes

With the departure of Mr Tony Latter, former Deputy Chief Executive (Development) in January 2003, the responsibilities of the post were temporarily taken over by the Deputy Chief Executive (Monetary), except for the Support Services Division, which was put under the schedule of Deputy Chief Executive (Banking) with direct supervision from the Executive Director (Banking Development). The opportunity was taken to reshuffle the duties among some departments:

- (a) Work relating to the development of Hong Kong's financial market was transferred from the Research Department to the Monetary Policy and Markets Department, which was retitled Monetary Management and Infrastructure Department (MID);
- (b) The two HKMA Representative Offices in New York and London were grouped under the External Department instead of MID to enable the adoption of a more proactive approach in supporting the HKMA's liaison efforts and research into international financial issues;
- (c) The Research Department expanded its role in research on the domestic and international economic environment to assist the HKMA's surveillance work and investment activities; and
- (d) The Reserves Management Department took over from the former Exchange Fund Investment Limited (EFIL) the management of the long-term Hong Kong equity portfolio.

Staffing

In early 2003, when the operations of EFIL were wound down, the 21 staff on secondment to EFIL were returned to the HKMA. In accommodating these staff, the overall establishment of the HKMA increased from 583 to 604. These staff provided the necessary resources for the management of the long-term Hong Kong equity portfolio and various new or expanded activities planned in 2003.

The establishment of the HKMA at the end of 2003 is shown in Table 1. In line with the HKMA's continuing efforts for cost efficiencies, savings were achieved by freezing the posts of a Deputy Chief Executive and an Executive Director, as well as six other posts in the supporting ranks, through natural attrition and work reprioritisation.

TABLE 1 HKMA establishment

Post	Establishment	
	2002	2003
Chief Executive	1	1
Deputy Chief Executive	3	3
Executive Director	9	10
Division Head	31	31
Senior Manager	71	74
Manager	143	147
Manager Trainee	6	6
Assistant Manager	94	94
Technical Officer	103	111
Clerk	43	45
Secretary	69	72
Office Assistant	10	10
Total	583	604

Remuneration of senior executives

In 2003 the HKMA continued to implement the framework approved by the Financial Secretary, on the advice of EFAC and its Remuneration and Finance Sub-Committee, as a result of the review conducted by the Hay Group Limited for the Government on the remuneration of senior executives of statutory and other bodies.

The pay adjustments for 2003 took the form of cuts in Fixed Pay of 2.11% for the Executive Directors, 3.14% for the Deputy Chief Executives, with the agreement of the individuals concerned. For the Chief Executive of the HKMA, the Fixed Pay was reduced by 5.24% in 2003; this was in addition to his voluntary cut of 10% in October 2001. The Variable Pay awarded to individual senior staff varies, as usual, according to performance.

Table 2 shows the remuneration packages of HKMA senior executives in 2003.

TABLE 2 Remuneration packages of HKMA senior executives in 2003

HK\$'000	Chief Executive	Deputy Chief Executive (average)	Executive Director (average)
Number of staff	1	4	9
Fixed pay	6,583	4,686	2,902
Variable pay	1,725	740	350
Other benefits	428	124	215

Notes:

- (a) Except for annual leave accrued, the actual remuneration received by staff not serving a full year is annualised for the purpose of calculating the average annual package of the rank.
- (b) The number of staff at the Deputy Chief Executive (DCE) rank reflects the departure of two DCEs and the arrival of one DCE during the year. The number of DCEs since January 2003 is two.
- (c) Other benefits include provident funds, medical and life insurance and annual leave accrued during the year. The provision of these benefits varies among senior staff depending on individual terms of service.

Training and development

The new training framework implemented since 2002 continued to work well. Staff members were provided with horizontal and vertical training in line with career development and organisational needs. Horizontal training, which is centrally co-ordinated by the Human Resources Division, caters for the needs common to staff of the same rank, and vertical training is initiated by departments to meet their specific needs.

In working out the training plan for 2003, the original intention was to attach equal weight to horizontal and vertical training. Following the outbreak of SARS, however, some overseas vertical training programmes were cancelled. To catch up with the lost training opportunities, some of the budget was reallocated to conducting in-house horizontal training programmes. A total of 3,741 training days was provided for HKMA staff in 2003, with 2,555 days on horizontal training. On average, each staff member received 6.39 days of training.

For the purpose of horizontal training, various training consultants were commissioned during the year to run tailor-made programmes for staff at different levels to improve their core competencies in the areas of personal effectiveness, leadership, communication and PC skills.

Vertical training programmes covered various topics on bank supervision to update staff on the current supervisory issues and banking operations and products. Most of these programmes were conducted by line staff, and topics included risk-based supervision, the New Capital Accord, stress testing, money laundering, deposit protection, credit reference agency and securities activities. Other programmes were on IT security, credit card operations and personal loans, which were delivered by guest speakers from commercial banks or corporations. On top of in-house training,

arrangements were made for staff to attend courses on central banking, economics, banking regulation and investment offered by other central banks, multilateral organisations and financial institutions.

Staff activities and voluntary work

HKMA staff participated in various community events and fund-raising activities during the year. An HKMA team participated in, and raised funds for, the Hong Kong Marathon and the Green Power Hike, which were both held in February. The Hong Kong Red Cross blood donation day in July was supported by 55 staff. Staff also participated in other fund-raising activities, such as the Community Chest's Skip Lunch Day, Green Day and Dress Casual Day.

The HKMA Volunteer Team participated in the Marine Park Ambassador Scheme and undertook more than 300 hours of voluntary service after office hours. The HKMA bought suitable office supplies from a workshop staffed by people with physical disabilities.



An HKMA Corporate Team participates in the Green Power Hike in February 2003.

FINANCE AND ADMINISTRATION

The Finance and Administration Division aims at achieving an efficient allocation of resources within the HKMA. One of the Division's major tasks during the year was to manage the relocation of the HKMA to its new office at Two International Finance Centre in November. The move was completed smoothly in November 2003 without any interruptions to normal operations.

During the SARS outbreak, the HKMA activated contingency arrangements and maintained split-team operations at both the main office and the back-up site from 8 April to 19 May 2003. The experience gained from the SARS outbreak has provided useful input in updating and improving the contingency plans.

Since the HKMA's Environmental Policy was issued in late 2001, a number of green office measures have been implemented and staff awareness of environmental issues has increased (Table 3). The HKMA continued to support and encourage recycling. Waste paper was collected for recycling. Obsolete personal computers and other computer equipment and peripherals were donated to charitable organisations. Regular campaigns were held to collect unwanted clothes, toys and other reusable items from colleagues for donation to people in need.

INFORMATION TECHNOLOGY

The Information Technology Division provides reliable and efficient IT services to all business units in the HKMA. During 2003 the Division continued its efforts to strengthen the HKMA's IT systems and infrastructure to facilitate all its operations.

Reserves and Monetary Management System

The Reserves and Monetary Management System project was initiated in 2000 to develop a fully integrated transaction system linking all major business processes covering front, middle and back office functions for the operation and management of the Exchange Fund. The new system went live in August 2003 and has been operating smoothly.

Relocation to Two International Finance Centre

A new computer centre and new network infrastructure were built in the new premises at Two International Finance Centre. The computer centre was designed to operate around the clock, comply with the Hong Kong Government's security standard (level 2) and achieve a very high reliability – an uptime of 99.99 per cent. The new network infrastructure was built with the latest proven technology, providing a highly reliable and secure

TABLE 3 A more environmentally-friendly office

Item	Unit	2001 Usage	2002 Usage	2003 Usage	Percentage change from 2002 to 2003	Remarks
Paper	ream	15,000	14,630	14,500	-0.9%	Increased use of single-side used paper and electronic communications
Christmas card	item	3,100	2,700	2,600	-3.7%	Increased use of electronic greeting cards
Paper cup	item	91,000	46,000	42,000	-8.7%	Increased awareness in reducing paper consumption
Waste paper collected	kg	36,595	28,789	46,901	+62.9%	Increased awareness in collecting waste paper for recycling

metropolitan network connecting Two International Finance Centre, the Quarry Bay Office and back-up offices. Both projects began in July and were completed in time for the relocation scheduled for November 2003.

In the first half of 2003 extensive discussions were held with business units to develop a plan for relocating servers, PCs and printers with minimal disruption to the HKMA's daily operations. Taking advantage of the new office layout, printers were re-shuffled to improve usability and efficiency while obsolete printers were retired to keep down the cost of maintenance. Contingency plans of all IT systems were reviewed and tested before the relocation. All IT systems were relocated smoothly in November 2003, providing a continuous and stable IT infrastructure for the HKMA's operations.

Use of Hong Kong Post e-cert in the Submission Through Electronic Transmission (STET)

Following the launch of the enhanced STET system in October 2002, which allows the use of digital certificates issued by Hong Kong Post's Certification Authority for electronic submission of banking returns, migration of all authorized institutions to the new system was completed in June 2003.

OFFICE OF THE GENERAL COUNSEL

The Office of the General Counsel (OGC) advises the HKMA on the legal aspects of all of its activities. The practice of the HKMA is to involve the OGC's lawyers at an early stage in the planning and implementation of projects, initiatives and operations.

On top of its general operational workload, the OGC was involved in a number of important projects in 2003, including the drafting of the Clearing and Settlement Systems Bill and Deposit Protection Scheme Bill and the preparation of the euro clearing system in Hong Kong. The OGC helped in the preparation of Memoranda of Understanding with other banking supervisors and in the amendments to the Banking Ordinance to prepare for the new supervisory regime for authorized institutions engaged in securities and futures activities. The OGC advised on a number of other projects, including personal renminbi business in Hong Kong, the New Basel Capital Accord, the creation of a commercial credit reference agency and several important bank mergers.

The OGC advised on these substantial projects from their inception, all of which involved complex issues of financial, regulatory and administrative law.

Lawyers from the OGC participated in meetings and conferences of interest for central bankers and their legal advisors to keep abreast of topical developments in major international financial centres. These functions covered issues such as money laundering, electronic financial infrastructure and payment and clearing systems. They took part in a series of teleconferences, and corresponded, with their counterparts from central banks and international legal think-tanks to clarify and resolve topics of current concern.

Presentations were also made at professional seminars on subjects ranging from corporate governance issues for banks, banking supervision, anti-money laundering measures and the prevention of terrorist financing.

INTERNAL AUDIT

The Internal Audit Division (IAD) was established in 1995 to assist management in controlling risks, monitoring compliance and improving the efficiency and effectiveness of control systems and procedures within the HKMA. The Chief Executive of the HKMA has granted an Internal Audit Charter to the IAD to formalise its role, mission and authority. The Division reports directly to the Chief Executive of the HKMA and the EFAC Audit Sub-Committee (ASC). Together they approve the annual audit plan prepared by the IAD, meet regularly with the Division and receive reports on the progress and results of its work.

 > [About the HKMA](#) > [Internal Audit](#)

Audit results in 2003

With the support of the HKMA Chief Executive and of the ASC, the IAD continued to operate independently throughout the year. The results of the audits conducted in 2003 were satisfactory. Recommendations for improvement put forward by the IAD were well received by auditees. Co-operation and assistance from the auditees and other HKMA staff contributed to another year of success for the work of the IAD.

The internal audits carried out during the year covered the HKMA's key functions, including monetary operations, reserves management, settlement operations, and finance and administration. Apart from the audits of internal control systems of individual business units, the IAD also reviewed the security management of various IT systems and advised on IT systems development projects such as the new Reserves and Monetary Management System. In addition, the IAD worked jointly with a professional accounting firm on a Value-for-Money audit to

assess the economy, efficiency and effectiveness of the use of resources within the organisation. The IAD continued to deploy various audit software, where applicable, in operational audits and system security reviews to increase the efficiency and effectiveness of its work.

To further improve risk-based management in the HKMA, the IAD developed a Risk Assessment Methodology (RAM) to provide management with a framework to systematically identify and assess risks and the corresponding internal controls. The HKMA's RAM was developed after a detailed study of the risk assessment models used by other central banks and professional firms and a trial application in a pilot risk assessment exercise. The RAM was launched for organisation-wide implementation in August 2003. With the input and support from management, the implementation exercise was largely completed by the end of 2003. It is expected that individual business units will complete the risk assessment exercise in the first quarter of 2004, followed by a review and consolidation exercise by the IAD.

The IAD attaches great importance to keeping abreast of the development of internal audit standards in the industry and the practices adopted by other central banks. During the year, the IAD met with internal auditors of the State Administration of Foreign Exchange, China and other regulatory authorities and institutions in the banking and financial industries to exchange views on risk management and internal audit approaches and to share practical experience. Training courses and seminars on audit techniques and language skills were arranged for the IAD's professional staff to facilitate their performance of audits and career development.