



**HSBC Investments**

**Impact of Pension Funds on  
Capital Markets  
(Hong Kong Experience)**

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### Agenda

- Pension funds as a saver
- Pension funds as an investor
- Pension funds as a product innovator
- Conclusions

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### **Pension Funds as a Saver**

**A vibrant capital market requires:**

- Active participants
- Means to satisfy the participants' needs:
  - Investment returns
  - Hedging mechanism
  - Capital raising
- Steady supply of innovative products

**Pension funds are one of the important participating groups.**

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### **Pension Funds as a Saver (2)**

**They are active participants because:**

- They form one of the largest pools of assets
- They are return seekers
- They are long term investors
- They have hedging requirements
- They represent collective wishes of their members / sponsors

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### **Pension Funds as a Saver (3)**

**Hong Kong Pension Funds have played a significant part in the region's capital markets:**

- First privately sponsored began in 1919
- The Occupational Retirement Schemes Ordinance laid the foundation of regulated and funded pension schemes
- The Mandatory Provident Fund regime in 2000 began the era of compulsory funded, members oriented savings programme

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### Pension Funds as a Saver (4)

Despite MPF, ORSO schemes remain a significant pool of assets:

	30/9/99	31/3/01	31/3/02	31/3/03	31/3/04
<b>Number of schemes</b>	17,529	14,627	7,462	6,603	5,941
<b>Number of members</b>	926,737	776,000	617,000	638,000	565,000
<b>Assets (HK\$m)</b>	136,531	178,178	157,445	156,718	177,714
<b>Annual Contributions (HK\$m)</b>	22,735	21,538	18,819	19,640	17,401

Source: Insurance Commission Annual Report, MPFA Annual Reports and Statistical Digest

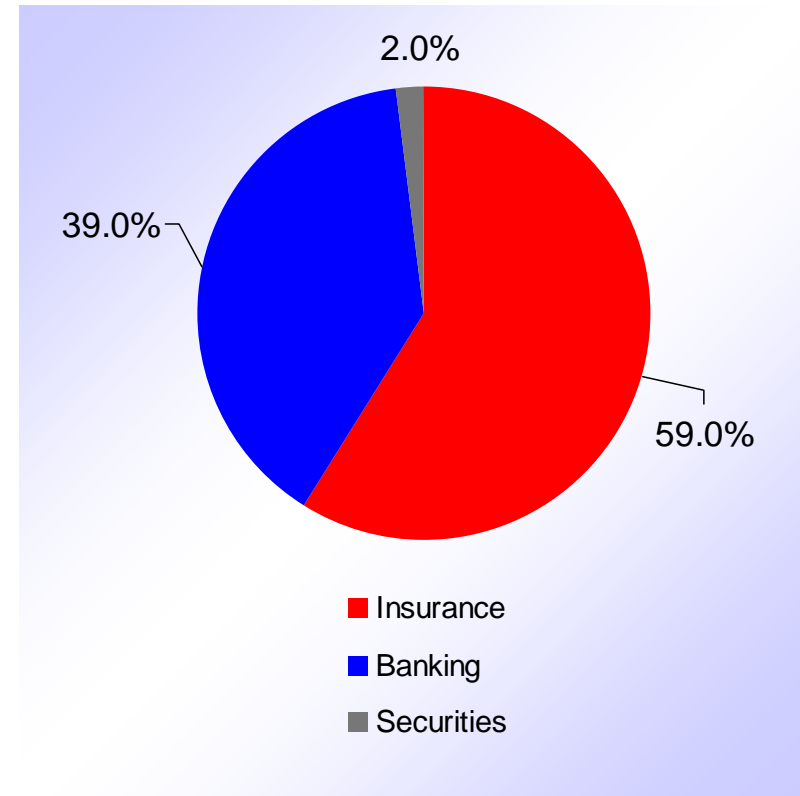
Notes: Daily turnover of the Hong Kong Stock Exchange is about HK\$10bn per day.

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### Market statistics

- As at end of 2004, MPF total asset size at HK\$120,183 million (US\$15,408 million)
- 19 companies provide MPF services to just over 2.2 million working population in HK with over 93% compliance rate
- The MPF Authority has registered a total of 24 639 MPF intermediaries, comprising of 437 service-providing companies and 24 202 individuals

Registered individuals by line of business

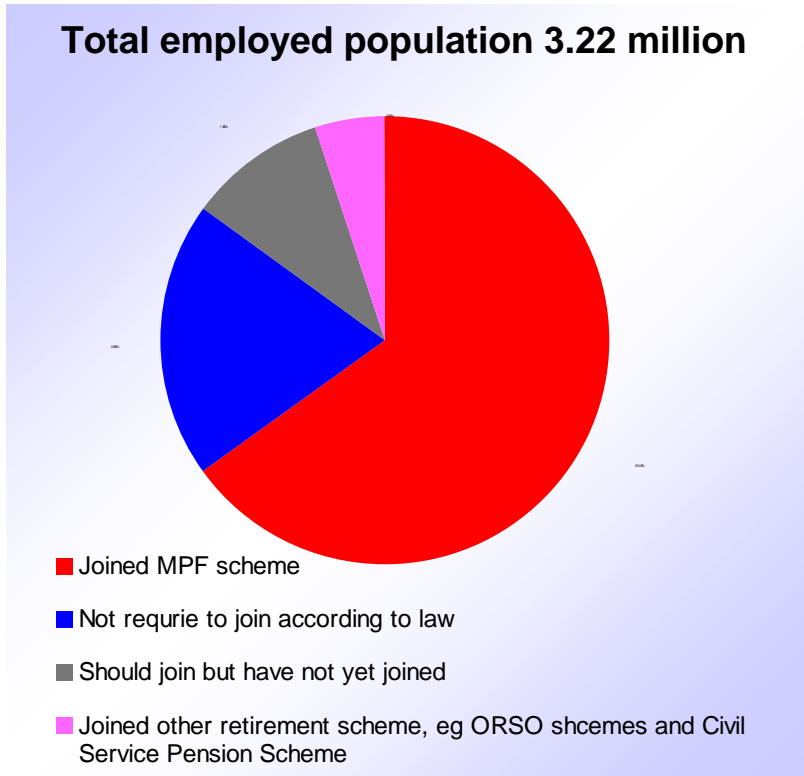


Source : MPF Schemes Statistical Digest, December 2004

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### MPF market

#### Employed population by type of retirement scheme



#### Number of MPF schemes

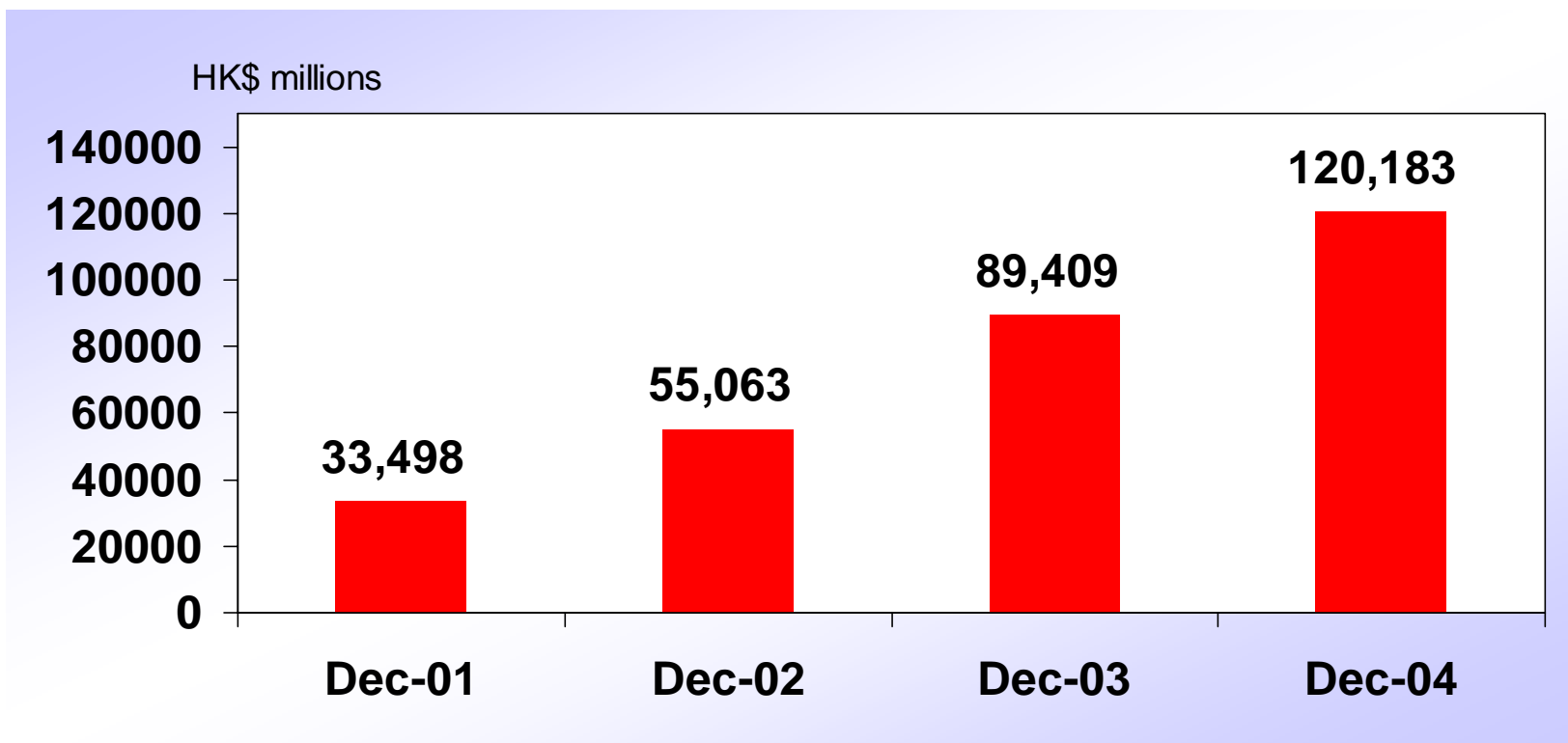
No. of scheme	
Master trusts	43
Industry schemes	2
Employer sponsored schemes	2
Total	47

Source : MPF Schemes Statistical Digest, December 2004



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### Growth in MPF assets



Source : MPF Schemes Statistical Digest, December 2004

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### Pension Funds as a Saver (5)

#### Conclusions:

- Pension funds represent a significant pool of assets
- Their continuity is guaranteed by legislative
- Overall assets under management will continue to rise
- These funds are very long term investors

## Pension Funds as an Investor

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### Pension Funds as an Investor

#### Peculiarities of the Hong Kong Pension Funds Investment Strategy:

- Domestic investments are limited to mainly local equity market
- Typical pension funds have significant exposure to equities
- Lack of a deep and liquid bond market has been handicap
- The currency peg means that the US markets have been acting as proxies. Will this last?

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### Pension funds as an Investor (2)

Common MPF funds and preference

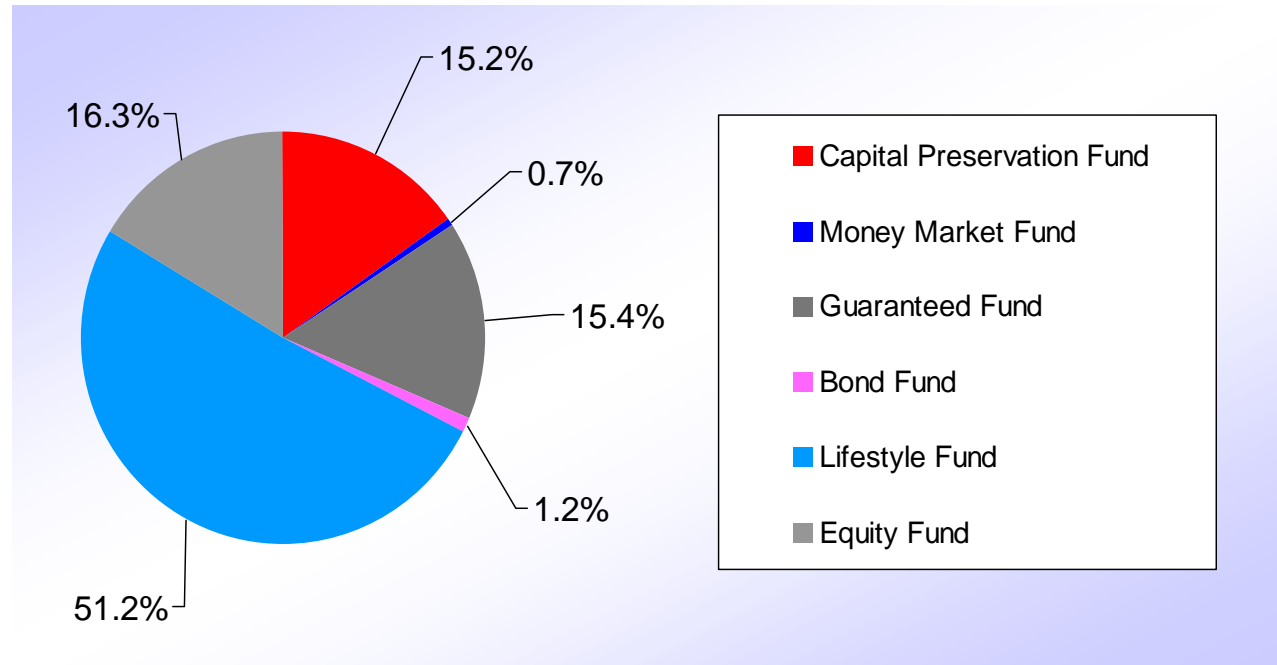
**Capital preservation fund – mandatory option, administration fee can only be deducted when returns exceed “prescribed savings rate”**

**Guaranteed fund**

**Bond fund**

**Lifestyle fund**

**Equity fund**



Source: MPF Schemes Statistical Digest, December 2004

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### Pension Funds as an Investor (3)

Benchmark asset allocation of life style funds:

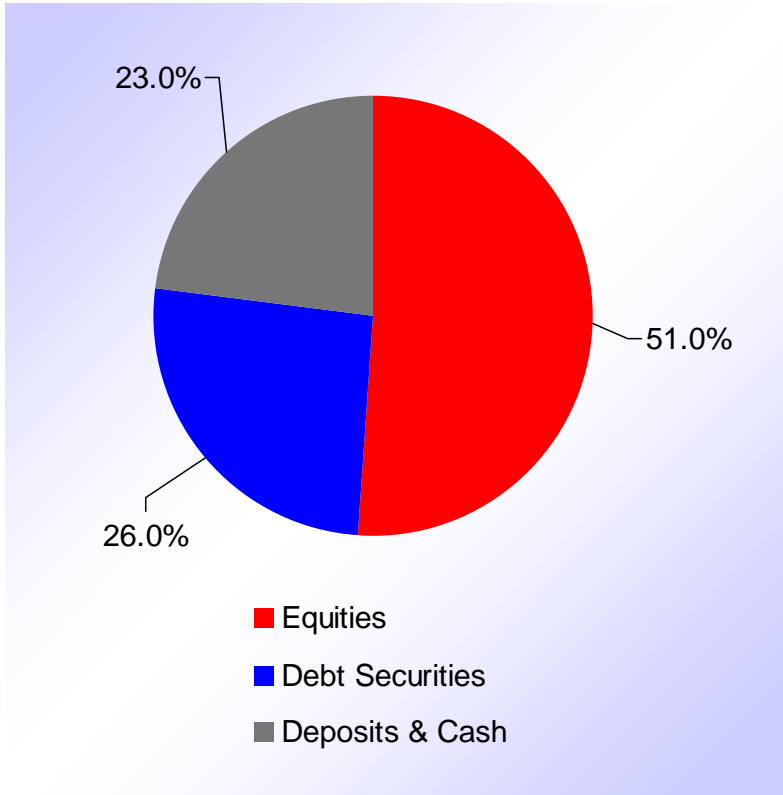
	Stable (30/70)	Balanced (70/30)	Growth (90/10)
<b>Equities</b>			
<i>Hong Kong</i>	10	24	30
<i>Asia ex Japan ex HK</i>	4	9	12
<i>Japan</i>	4	9	12
<i>Europe</i>	6	14	18
<i>US</i>	6	14	18
<b>Bonds</b>	60	25	7
<b>Cash</b>	10	5	3

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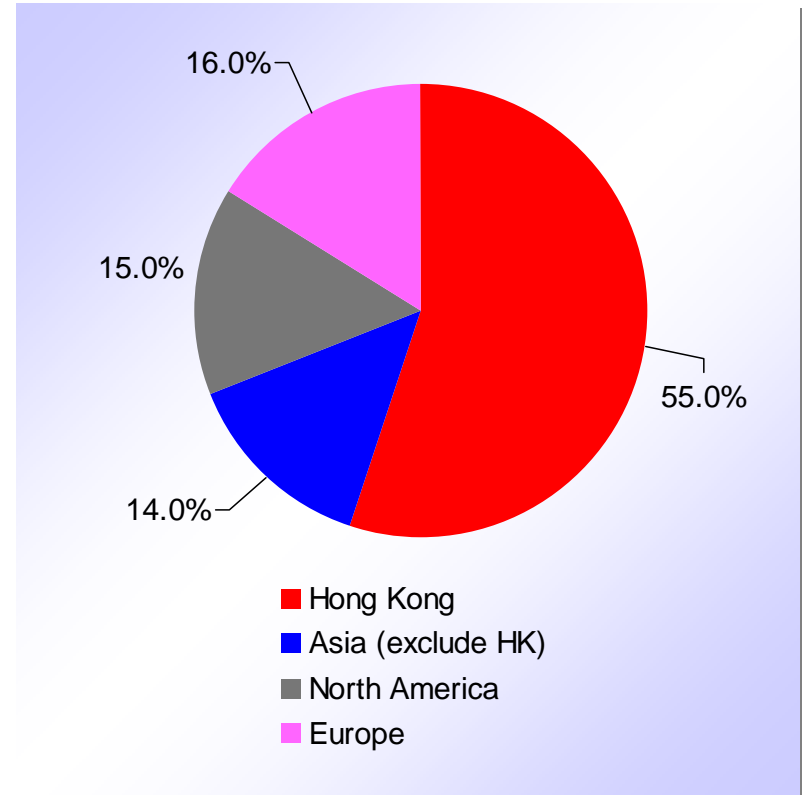
**Pension funds as an Investor (4)**

All MPF funds asset allocation

By asset class



By geographical region



Source: MPF Schemes Statistical Digest as at end of September 2004

## Pension Funds as a Product Innovator



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# Pension Funds as a Product Innovator

### Two main areas of innovation:

- New investment vehicles
- New fund options for Members Choice Programme

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# Pension Funds as a Product Innovator (2)

### New investment vehicles – recent examples:

- Hedge Funds
  - Investments in these funds provide credibility to the asset class
  - New asset allocation tool
- Funds of Funds
  - Departure from traditional investment arrangements
  - Is this the new paradigm?
- Hong Kong Dollar Bond
  - Very little exposure
  - Poor liquidity and supply
  - Natural demand due to currency matching benefits
  - Form anchored investors for new product in this area

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### Pension Funds as a Product Innovators (3)

#### Demand for new products:

- Investments are driven by individual members
- Currently conservative products dominate the choices
- As members become more knowledgeable, more “risky” and sophisticated products will be picked
- REITs? Hedge Funds?
- Legislative changes may be necessary

## Conclusions

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### Conclusions

- Due to its nature, Hong Kong pension funds will become a stabilizing factor in the local capital markets, both equities and bonds
- There will be continuous demand of innovative investment vehicles and investment products
- MPF is 3 years old, the regime will get to a stage for revamp
- So far, the system has resisted attempts to weaken its position
- Beyond capital markets, pension funds also have profound impact on the financial services industry

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