



SECURITIES AND  
FUTURES COMMISSION  
證券及期貨事務監察委員會

## Post-crisis Regulatory Reform in Financial Markets and its implications for Asia

10 February 2012

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### Asian perspective – post-financial crisis regulatory reform

- Asian financial markets & institutions were not as impacted by the global financial crisis in 2008.
- However, Asia is not immune to effects of the financial crisis, which has highlighted the following areas of weakness:
  - Selling of complex investment products to retail investors
  - Trading of OTC derivatives
  - Trading in overseas markets



## Selling of complex investment products to retail investors

- **Financial crisis exposed the following issues relating to selling of complex investment products :**
  - Growing **complexity of financial products** and product innovation **make associated risks less apparent** to investors
  - **Insufficient product disclosure** to help investors make investment decisions
  - Intermediaries **recommending unsuitable investment products** to investors
  - Intermediaries **not acting in the best interests** of their clients



## Regulatory response

- **IOSCO Initiatives**
  - Point of Sale Disclosure principles
  - Suitability Project
  - Investor Education Project
- **HK SFC Initiatives**
  - **Restriction on the use of gifts** to promote a specific investment product



- **Key Facts Statement (KFS)**
  - *KFS templates to help investors understand the **key features** and **risks of investment products***
- **Investor Education**
  - *Learn Before You Invest*



## Trading of OTC derivatives

- **Financial crisis highlighted weaknesses in the structure of OTC derivatives markets that contributed to the build-up of systemic risk:**
  - Build-up of large counterparty exposures not appropriately risk-managed.
  - Opaque nature of OTC derivatives market and increasing complexity of products facilitated excessive leveraging and risk taking.
  - Potential for contagion arising from the interconnectedness of OTC derivatives market participants transacting globally.
  - Limited transparency of overall counterparty credit risk exposures precipitated a loss of confidence and market liquidity in time of stress.
- **G20 Leaders called for reforms in OTC derivatives market as part of a broad-ranging package of measures designed to strengthen the financial system.**
- **The reforms present a number of challenges and opportunities for regulators and markets eg. potential for greater market integration.**



## Regulatory response

- **Challenges**
  - Ensuring **international consistency** to avoid unlevel playing field and overlaps in regulation – working groups have been set up to facilitate international cooperation and develop standards in key areas.
  - **Balancing domestic policy considerations**, such as effective oversight of CCPs and access to data (especially in crisis situation) with desire to **facilitate market integration** and **efficiency**.
  - **Timing** – significant legislative and operational changes required to meet G20 target timeframe of end 2012.
- **Hong Kong initiatives**
  - **Active engagement** in international working groups and taskforces, eg SFC Deputy CEO co-chairs the BCBS / IOSCO / CPSS / CGFS working group on margin standards for non-centrally cleared derivatives.
  - **Consultation with industry** on key aspects of new OTC regulatory regime.
  - Establishment of **trade repository** and **new clearing house** in progress.



## Trading in overseas markets

- The collapse of **Lehman Brothers** and **MF Global** highlights the risks for local investors that trade in overseas markets via overseas 3<sup>rd</sup> party intermediaries.
- Many **local client assets** are **frozen overseas** as liquidators of the failed overseas intermediary need time to calculate client exposures and return client money. This may create **liquidity pressure** on local brokers and their clients.



## Regulatory response

- The IOSCO Report on Survey of Regimes for the Protection, Distribution and/or Transfer of Client Assets (March 2011) highlighted:
  - the importance of segregation of client assets; and
  - importance of efficient transfer of client assets back to clients in the event of investment firm failure, to reduce client exposure and liquidity pressure.
- In Hong Kong, intermediaries are required to:
  - Evaluate and monitor the risks associated with their relationship with **overseas counterparties**; and
  - provide investors with **additional risk disclosure** about conducting **transactions in overseas jurisdictions**.

