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Analysis: Why Short-Term Financial Products Lack in Hong Kong

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Abstract

As one of the three major financial centers in the world, Hong Kong has a wide range of financial products in the market. However, there is a scarcity of short-term (less than five years) investment products (Sun, 2022). Through data collection, reasons analysis, and results exposition, the current study investigates and summarizes various reasons behind this phenomenon, such as sequelae of "Black Swan" Events, historical factors, low deposit interest rates, etc. The article aims to elucidate the impact of the lack of short-term financial products in the local financial landscape and explore potential solutions to address those issues. These analytical findings will help policymakers, financial institutions, and citizens of Hong Kong to have a more comprehensive understanding of the challenges and opportunities in Hong Kong's financial industry.

Keywords: Hong Kong financial market, short-term financial products, interest rates and risks

1. Introduction

Hong Kong is a world-renowned financial center and has an extremely developed and mature financial market. Improved financial regulations have ensured the operation of its financial market. Nevertheless, in Hong Kong, short-term financial products rarely exist. In mainland China, low-risk, and fixed-income short-term financial products such as Yu'E Bao and Mini Fund have been widely spread and used. Many seven-day financial products have also been booming. Once the Central Bank's short and medium bonds were issued, they were snapped up. But in Hong Kong, finding traces of short-term financial products is difficult. The purpose of the current research is to explore the reasons for the lack of short-term financial products in Hong Kong by analyzing the situation of Hong Kong's financial and capital market. Methods of the research are primarily integrating data, consulting literatures, and then analyzing. The article also presents some prospects and rational suggestions for the future of short-term financial products in Hong Kong.

2. Literature Review

Hong Kong is one of the world's three recognized international financial centers. Nevertheless, in recent years, it is inclined that the amount of short-term financial products is declining in Hong Kong. Comparing the financial products of Hong Kong and mainland China, it is discovered that the term base of financial products in Hong Kong is too high, such as the persistently low-interest rates of the banks attached, the difference in investment concepts shaped by the changes in the regional environment, the traditional rules and regulations of the market, etc., which contribute to the difficulty of discovering more short-term financial products in Hong Kong nowadays (Sun, 2022).

Besides, in Wang and Lei (2023), they surveyed this topic via predominantly researching on a large amount of literature. They analyzed the population basis of Hong Kong and concluded that the phenomenon is largely attributed to the investment philosophy of Hong Kong citizens. Zhang et al. (2023) analyzed from the perspective of the supply-demand relationship and some external factors, such as the holding period and motivation for the development of the money fund and the regulatory system in Hong Kong.

However, these papers are not comprehensive because most tend to be restricted to a certain point. The current article, combined with the background and latest economic situation in Hong Kong, integrates points from the literatures, analyzes data, and proposes feasible solutions to confront the potential problems brought by the phenomenon.

3. Reasons of Why Short-Term Financial Products Lack in Hong Kong

3.1 Offset "Black Swan" Events

Compared with long-term financial products, short-term funds are more vulnerable to market influences and generate interest rate fluctuations. Therefore, short-term funds are more uncertain and riskier.

In recent years, the so-called "Black Swan" Events have occurred frequently. For example, due to the outbreak of the COVID-19 pandemic, the US stock market experienced circuit breakers, and the Hong Kong stock market plummeted. HSBC canceled the distribution of the fourth dividend for 2019, and the company's stock price plummeted by 10% on that day. There are many other examples, such as the financial fraud of Luckin Coffee, the scam of Crude Oil Treasure... These emergencies suggest that financial events can have a significant impact on markets in a short period of time. However, the financial market is a long-term situation of dynamic fluctuations. As the timeline extends, these sudden impacts will be smoothed out, and the losses of buyers will be minimized or even eliminated.

Take US stocks as an example. During the COVID-19 pandemic, the US stock market triggered four circuit breakers within ten days. The stock prices had fallen historically, and the US financial market faced a severe crisis. But now, in 2023, The stock prices of US stocks have returned to normal levels and have even improved compared to five years ago (Figure 1).

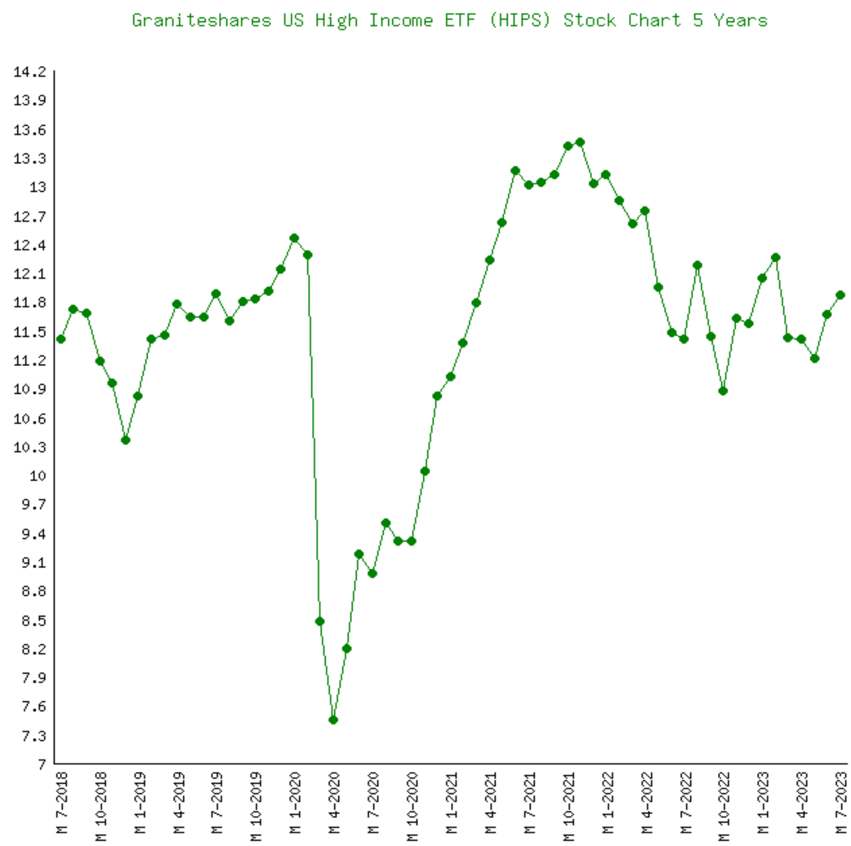

Figure 1. The historical 5-year price chart of Graniteshares US High Income ETF (HIPS)

Source: https://www.netcials.com/stock-price-chart-history-nyse-american/HIPS-Graniteshares-US-High-Income-ETF/.

That is also why most of the financial products in Hong Kong have a minimum duration of five years. Some funds have poor calendar year performance, but in the long run, their cumulative performances are great (Fig. 2).

Figures as of 30 June 2020 資料截至2020年6月30日

Name of Investment Options 投資選擇名稱	Code 代號	Bid Price per unit 每單位之買入價	Underlying Funds Size (in million)[1] 連繫基金總值(百萬)[1]	Cumulative Performance (%)[1] 累積表現率[1]					Calendar Year Performance (%)[1] 年度表現率[1]					Risk Level[2] 風險類別[2]	Overall Morningstar Rating[3] Morningstar 綜合星號評級[3]
				YTD 年初至今	3mths 三個月	1 yr 一年	3 yrs 三年	5 yrs 五年	2015	2016	2017	2018	2019		
				Performance figures are calculated on the basis of net-asset-value to net-asset-value in USD with dividend reinvested. 表現數據以美元幣別的淨資產總值比淨資產總值及將股息再作投資計算。											
Franklin Templeton Investment Funds - Franklin Gold and Precious Metals Fund A "Acc" [7] 富蘭克林鄧普頓投資基金 - 富蘭克林黃金及貴金屬基金A股 (累算) [7]	D14	US$美元 6.53	US$美元 312.16	18.94	68.73	46.09	38.94	74.13	-21.37	52.35	-1.10	-18.04	49.18	High 高	★★★
JPMorgan Pacific Technology Fund [7] 摩根太平洋科技基金 [7]	F05	US$美元 84.36	US$美元 180.14	16.68	31.71	41.45	35.87	84.76	1.08	14.48	48.35	-26.75	37.95	High 高	★★
Allianz Oriental Income "AT" 安聯東方入息基金 "AT"	P03	US$美元 180.54	US$美元 423.14	14.05	40.15	41.38	49.61	67.93	-0.79	2.13	34.06	-19.53	39.37	High 高	★★★★★
Value Partners Chinese Mainland Focus Fund Value Partners 中國大陸焦點基金	V03	US$美元 69.62	US$美元 137.96	19.07	25.55	37.43	48.57	38.57	1.70	-10.33	61.19	-28.32	36.58	High 高	★★★★
BlackRock Global Funds - World Gold Fund "A2" 貝萊德全球基金 - 貝萊德世界黃金基金 "A2" 股	I07	US$美元 41.75	US$美元 6038.14	24.22	52.48	36.75	40.01	77.36	-21.88	50.92	2.68	-17.58	34.55	High 高	★★★★

Figure 2. Fund returns rate of five investment options

Source: Adapted from John Chen's Lecture 4.

3.2 Effects of Historical Factors

Before the return of Hong Kong to China, it was under British rule for a long time, and freedom and laissez-faire became the most essential labels of its financial market. It implemented low tax rates and a simple tax system for fiscal revenue, and fiscal expenditure adhered to the basic financial concept of "active non-intervention". The financial market in Hong Kong, which grew and developed during its colonial history, has difficulty eradicating the conservative financial concepts and the market order that has formed as a result (Baker & Wurgler, 2006). Hong Kong ranks top in economic freedom, with minimal government intervention, and mainly relies on market self-adjustment. Under such historical and market circumstances, it is not conducive to the emergence of short-term financial products.

3.3 High Financial Threshold and Handling Fees

In Hong Kong, the threshold and transaction fees for investment are very high, which is not conducive for ordinary people not knowledgeable about financial management to purchase high-risk short-term financial products. Though becoming a private banking client can receive recommendations from product managers for financial products, the threshold is as high as 10 million US dollars, and many Hong Kong citizens do not have that much disposable capital. At the same time, handling fees are also significant expenses. For example, purchasing short-term financial products at HSBC requires paying a large proportion of handling fees. If the subscription amount is within HKD 1 million, a 2% transaction fee will be charged. For most banks, the operating expenses of funds can be as high as 7%, even with a 1% to 3% reduction based on customer level (Zhang et al., 2021). In addition to fund management fees, they still account for a large portion of the returns, resulting in very low expected returns for clients. The high threshold and significant proportion of purchasing transaction fees set by banks have suppressed the demand for short-term financial products among Hong Kong citizens.

3.4 Extremely Low Deposit Exchange Rate

The exchange rate in the Hong Kong financial market is very stable, adopting a US dollar peg system. The value of the Hong Kong Dollar (HKD) is stable as well, leaving little room for investment. The deposit interest rates in banks are meager and fully market oriented. For deposits over HKD 1 million and with a deposit period of 12 months, most banks offer interest rates ranging from 0.3% to 1%. For example, HSBC offers 0.8% (HSBC HK, 2023), and Standard Chartered Bank offers 0.875% (SCB HK, 2023). In Hong Kong, some banks will charge a monthly management fee if the account balance falls below the minimum deposit requirement. For instance, a handling fee in HSBC will be charged if the deposit amount in a wealth management account is below HKD 10,000 or its equivalent in RMB. Therefore, there is no opportunity for capital to gain interest rate differentials and no demand for short-term financial products. Investors will then shift their focus to funds such as stocks or bonds.

3.5 Gaps in Internet Financial Products

The level of electronic payment circulation in Hong Kong is lower than that in mainland China. Most areas still use cash settlement, and similar to European and American countries, they prefer credit cards and checks. Therefore, the popularization of some financial products like Yu’E Bao of Alipay and Mini Fund of WeChat in Hong Kong is far behind that in mainland China, with greater difficulty and higher promotion cost. The lack of Internet financial products makes it difficult for investment in Hong Kong to popularize and benefit the general public like in mainland China (Chen & Zhang, 2023). This is both a challenge and an opportunity for Hong Kong.

3.6 Investment Psychology of Hong Kong Citizens

Due to the limited development time and conditions of investment and financial management in mainland China, the general public need to gain financial management knowledge and the concept of asset allocation and risk diversification. Products like Yu'E Bao and Mini Fund meet the demand for liquidity and yield. In contrast, Hong Kong citizens, who possess a large amount of assets, need wealth preservation and appreciation. They prefer to pursue higher and more stable returns rather than seeking capital preservation. However, short-term financial products are highly unstable and volatile, failing to meet the wealth distribution requirements of most Hong Kong citizens.

In terms of those wealthy families who can buy land and houses in Hong Kong, they tend to invest in large-scale private-equity funds or more stable long-term financial products and trust funds. It follows that short-term financial products are not the top choice for either ordinary citizens or the affluent.

3.7 Strict Regulatory Systems

Compared to mainland China, the financial market in Hong Kong is more mature and well-developed, such as its regulatory system. However, this has also become the main reason for restricting the emergence of more diverse wealth management products. Hong Kong's strict regulatory system limits the launch of high-yield fund products. At the same time, the lag in developing e-commerce platforms has also led to banks being the primary subscription channel.

4. Conclusion

The previous section analyzes why Hong Kong lacks short-term financial products from various perspectives. “Black Swan” Events have made citizens more conservative in their financial concepts, unwilling to try short-term financial products with high risks and volatility. Before the return of Hong Kong, the British government's free market system and the government's basic non-intervention made it difficult for short-term financial products to emerge. High investment thresholds, transaction fees, and low deposit interest rates, make people unwilling to purchase short-term products. The lack of popularity of Internet financial products constrains the choices of Hong Kong citizens. They could only purchase products from banks. Regulatory systems are too strict to encourage the emergence of new short-term financial products. In addition, the cultural preferences of Hong Kong people for long-term investments and their conservative attitude towards financial planning further suppress the demand for short-term financial products.

5. Discussion

Hong Kong's financial market system is very different from that of the Chinese mainland, while it can draw on the mainland's advanced experience and focus on self-innovation. Hong Kong SAR follows the capitalist path, totally different from the mainland. Therefore, the pillar industries of the two regions will indeed be different. Hong Kong should make good use of the excellent investment environment, unrestricted capital withdrawal and deposit, and the freedom of entry and exit to attract home and abroad investors to invest in Hong Kong and further improve short-term financial products in the financial market (Fong et al., 2022). Concerning the current development status of the Hong Kong financial market, some suggestions have been put forward.

i. Increase the research and development innovation of short-term wealth management products and promote the deep development of both onshore and offshore funds.

ii. Expand subscription channels and develop online internet financial platforms, such as promoting some short-term financial products on Alipay HK.

iii. Adopt a more flexible operating system. Strict financial regulatory systems are necessary, but when people realize that the system is hindering the emergence of more diversified financial products, people responsible for formulating the systems are obliged to promote institutional innovation, learn from successful cases of excellent international markets, explore new methods and systems to better integrate into the global market in the new era, and develop the short-term financial products markets. Regulatory agencies need to further relax the regulation of interest

rates and exchange rates, promoting interest rate marketization and liberalization, and in turn promoting the development of the financial system and the real economy.

iv. Seize the opportunities brought by COVID-19 pandemic and the economic policies of the Guangdong-Hong Kong-Macao Greater Bay Area, and integrate the financial industry with technology, better serving the development of the real economy in the future.

v. Actively explore mixed operations so that commercial banks and other financial enterprises can conduct multi-business, multi-variety, multi-mode cross-operations and services in the currency and capital markets in a scientific organizational manner. With the development of the financial industry itself and the continuous improvement of the internationalization of the financial market, mixed operations is more suitable for developing the financial industry in Hong Kong. The limitations of the separate operations have created obstacles to the development of short-term financial products. Therefore, the banking industry should actively promote the process of changing the separate operations to mixed operations, and explore the methods to promote the development and prosperity of the short-term financial product markets.

In short, regulators, financial institutions, and society should work together to overcome the current restrictions and create a favorable environment for the development of short-term financial products in Hong Kong. Only in this way can Hong Kong better meet the diversified financial needs of its citizens and maintain its status as a major global financial center.

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