

**HKCBA Luncheon Keynote Speech (Draft)
By Stanley Kwan
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The Origin of the Hang Seng Index and Hong Kong in Transition

Mr. President, Distinguished Guests, Ladies and Gentlemen:

Thank you all for coming. And I would like to thank the Hong Kong Canada Business Association for hosting this event.

Two thousand and nine is a special year. It marks the 60th anniversary of the founding of the People's Republic and the 30th anniversary of China's "Reform and Opening".

This year is also special for me for another reason: it marks the 40th anniversary of my work compiling the Hang Seng Index.

Many of you may not know: the Index was launched on November 24, 1969, starting at One Hundred and Fifty-eight points (158).

Thirty-eight years later, on October 30, 2007, it reached a record high of nearly Thirty-two thousand points (31,958). However, by the end of 2008, the picture had changed. The Index had dropped back to the Fifteen thousand points (15,000) level because of the global financial crisis.

When I had my book launch in Toronto last December, someone in the audience asked me where I thought the market was going. I really didn't know. But I told him what I learned Forty years ago: what goes down will come up again.

And I was right, probably sooner than I thought. The Index is now at the Twenty thousand points (20,000) level again.

The person who taught me my first lesson on the market was Ho Sin Hang, the former chairman and co-founder of Hang Seng Bank.

In 1969, Chairman Ho decided that he wanted an index to measure the performance of the Hong Kong stock market. An active player in international markets, he wanted something like the "Dow Jones Industrial Average" for Hong Kong.

Some people in the bank had their doubts. "Hang Seng is only a small Chinese bank. We believe a large international bank is in a better position to compile the index," they said. But Chairman Ho was the boss, and he called the shots. Since I was heading the bank's Research Department, he gave me the task of compiling what came to be called the "Hang Seng Index."

Chairman Ho was a shrewd businessman with a bold vision.

If you remember, this was 1969, scarcely more than a year after the devastating riots of 1967, which was inspired by the Cultural Revolution on mainland China.

The Hong Kong economy had hit rock bottom. But Hang Seng Bank stayed put throughout the crisis. Chairman Ho told us: "What comes down will go up again."

His prophecy came true. As calm returned to Hong Kong, capital and emigrants came back, and the property and stock markets picked up. The launch of the Hang Seng Index was timely, and it gave the bank a lot of publicity and advantage in a fast growing market.

The story of Hang Seng Bank is the story of Hong Kong Chinese businessmen, who successfully transformed themselves and adapted to the global market. Like my father and my uncle, Ho came to Hong Kong from Guangdong Province in the early part of the 20th century and set up traditional Chinese banks called Yin hao. The Yin hao traded in gold and silver and handled foreign exchange and remittances for Chinese merchants. Our family Yin hao went bankrupt after the war. But Hang Seng successfully transformed itself and became a commercial bank in 1952.

This was a timely move. During the 1950s, many mainland industrialists and over a million refugees came to Hong Kong. This created the conditions for setting up factories and manufacturing for exports. Hong Kong was transformed from an entrepot to a manufacturing centre. Bank financing was in great demand, and Hang Seng Bank grew rapidly.

During the early 1960s, however, over expansion of bank credits and the collapse of the property market led to a series of bank runs. Hang Seng Bank itself suffered from an extended bank run in 1965. This only ended after the Hongkong and Shanghai Bank (now HSBC) acquired 51% of Hang Seng's shares. Then came the riots of 1967.

So, the Hang Seng Index was launched after a series of financial disasters. Its creation testifies to the optimism and vision of Chairman Ho for the future of Hong Kong.

Since its launch, the Index has seen some violent fluctuations. Each cycle reflected a major economic or political crisis that Hong Kong has had to face. But each time, Hong Kong was able to bounce back.

I witnessed two major cycles before I retired in 1984.

The first cycle was during the early 1970s. The Hang Seng Index soared to a high of Seventeen hundred (1,770) points in March 1973 following a period of over speculation, and then crashed during the world oil crisis that followed. It hit a low of only One hundred and fifty points (150) in December 1974 – even lower than its starting point.

The second cycle was from 1975 to 1983. With China's Reform and Opening in 1979, Hong Kong manufacturers were able to relocate their factories to the nearby Shenzhen Special Economic Zone, and cities in the Pearl River Delta. This helped them remain competitive despite rising land and labour costs in Hong Kong. As manufacturing moved north, and capital flowed in, Hong Kong transitioned into a financial centre. In July, 1981, the Hang Seng Index soared to a new high of Eighteen hundred (1,810) points.

But this sweet dream did not last long. The Sino-British talk on the future of Hong Kong began in July 1983 and reached an impasse in September. With a loss of confidence, Hong Kong's exchange rate depreciated more than 50% against the US Dollar and the Hang Seng Index plummeted to Six hundred and ninety (690) points in October. The Index only recovered after the pegging of the Hong Kong Dollar and the signing of the Sino-British Joint Declaration the following year.

As the Chinese economy expanded rapidly during the 1990s, Hong Kong benefitted as a financial centre. On June 27, 1997, at the junction of Hong Kong's return to Chinese sovereignty, the Index closed at a high of more than Fifteen thousand (15,196) points – almost 100 times its starting point. But then came the Asian financial crisis. And you are no doubt familiar with the most recent boom and bust cycle we are in today.

In conclusion, I would say that, as the rise and fall of the Hang Seng Index indicate, Hong Kong has had its share of economic ups and downs. And both China and Britain have played major roles in influencing Hong Kong's fortunes. Hong Kong is a great city full of opportunities and a city of risk-takers. And the stock market has always bounced back quickly after each crisis. The fact that Hong Kong has had to live under the shadows of two giants – China and Britain – has been a blessing in disguise.

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The title of our book is “**The Dragon and the Crown**” because, even though it’s a personal history, it is really a story of how Hong Kong has developed during the past century in between two giants: mainland China (the Dragon) and Britain (the Crown).

As you can gather from my uncle’s talk, Hong Kong’s development was heavily influenced by events in China. But if we look back into the past, we can see some of the new issues in a better perspective.

Over the years, mainland China has supplied Hong Kong with most of its labor force. Hong Kong had about one million people after the war, but the influx of refugees after the Communist Party took power in 1949 quickly doubled its population to 2 million by end 1950. Since then, about one million people came to Hong Kong from the Mainland every 10 years. You can imagine the demand this has placed on Hong Kong for housing, education and welfare. But, up to the late 1970s, this was also a blessing in disguise. Labor was cheap and in abundant supply, which allowed Hong Kong to become a major manufacturing and export center (one of the Four Little Dragons of Asia together with S Korea, Taiwan and Singapore). However, this can also be a double-edged sword. During the past two decades, Hong Kong has successfully transitioned into an international financial centre. Now it is trying very hard to maintain a competitive edge within a rapidly developing Chinese economy and the international market. But even though there are no more refugees as such, the continued influx of people from the Mainland for the purpose of family reunion has become a problem for Hong Kong. At the officially agreed rate of 150 per day (or over 50,000 per year) this steady inflow of mainly unskilled labor is taxing its resources and working against Hong Kong’s efforts to upgrade itself and remain competitive.

What the Mainland has always offered is, of course, business opportunities. During the Korean War, the opportunity to bypass the UN sanctions against China enriched quite a few businessmen. And until the 1980s, Hong Kong was the mainland’s primary window on the world. Trading companies reporting to MOFERT used Hong Kong as their base for imports and exports. But it was a narrow window, until the reform and opening of China’s economy in 1979 which allowed more mainland companies to open offices in Hong Kong. Now, of course, with the constant flow of goods, capital, services and people across the border, and one of the fastest growing economies of the world, the mainland market has become quite indispensable for businesses in Hong Kong. For better or worse, both the stock and property markets are heavily influenced by the flow of capital from the Mainland. Since the 1990s, the stock market has greatly benefitted from the fund raising activities of mainland companies. The property market has received support from mainland buyers. Recently, it was estimated that over 40% of luxury apartment buyers were from the Mainland. Within one year, prices in this market segment has rebounded back to close to the pre-crisis level (HK\$15,000 or C\$2,000 per sq ft) with some phenomenal record high prices. The Chief Executive told us last week that we could ignore the price increase in this segment because prices in the other segments were stable. But there is concern that we might be seeing another asset bubble, both in Hong Kong and on the Mainland.

In the area of politics, of course, the Mainland has always played a major role in Hong Kong. The underground Communist Party has been active in Hong Kong since its inception in the 1920s. Its influence was very visible at times, such as: in the resistance movement during the Japanese occupation, in cultural activities and education right after the war, behind the “riots” of 1967 during the Cultural Revolution, and in left-wing labor unions throughout. Today, of course, the mainland government is officially represented in Hong Kong. But the Communist Party remains underground, and this has become somewhat of a problem, with rising speculations about which political figures were party members and would surely toe the line of the mainland government.

It is in the underlying area of history and culture, however, that Hong Kong’s ties to China are the strongest (and for most overseas Chinese. Many traditions which were discouraged on the Mainland were preserved in Hong Kong, for example: paying respects to ancestors on Chung Yang and Ching Ming festivals. These are only being revived now on the Mainland. Hong Kong people were also highly patriotic throughout the Anti-Japanese War and the Second World War;

many contributed money, supplies and even their own lives and services. But since 1949, there has been an ideological split among the Hong Kong people, between those who support the mainland government and those support the Kuomintang government in Taiwan. Patriotism has different meaning for different people, and in the past the colonial government had discouraged any discussion of this issue. Today, of course, the situation has changed. The SAR government places much emphasis on education in patriotism and on learning about China. So, after more than half a century, many things have come around in a full circle.

In many ways, though, Hong Kong has benefitted from the legacy of both China and Britain. On the one hand, we have inherited a rich culture and history from China, which give many people a deep-rooted identity and sense of pride. On the other, we have inherited many modern institutions and a sound government and legal framework from the British. This has helped to solidify Hong Kong's position as an international financial centre and allows it to continue to play a meaningful role in China's development. We can all agree that, after more than a century of British rule, Hong Kong has inherited a good infrastructure. But more important, Hong Kong has developed good management skills and a sound respect for the rule of law. These factors, together with an active civil society (that has grown rapidly over the past few years), will allow Hong Kong to stay at the forefront of global development.

In recounting Uncle Stanley's personal experiences over the past 80 years and our family history, our book has tried to capture all these forces that played a role in shaping our lives and making Hong Kong into what it is today.

Synopsis of book (for reference):

- We started by looking at our roots as a traditional banking family. Our yinhao were in Sheung Wan (west of Central) where Chinese businesses were concentrated (and where our business revolved around trading on the Gold and Silver Exchange). We described life in my grandfather and my great grandfather's household before the war (including the central role of ancestor worship, and large family mansions where wives and concubines lived with their children in different wings);
- We talked about the surge of patriotism during the war (protests against Japanese goods; student activities to raise money; my uncles escaping with our relatives to the Mainland during the Japanese Occupation; and my uncle joining the Nationalist army as a wartime interpreter for US forces);
- The book also touched on the post-war activities of the Chinese Communist Party and the ideological split within the family (two of my uncles were recruited by the CCP through student activities and went back to the Mainland in 1949);
- Through my uncle's personal experiences and observations, we traced the structural changes in Hong Kong's economy, as we have already discussed: transitioning from an entrepot to a manufacturing centre after the war (as Hang Seng Bank changed from a yinhao to a commercial bank); and then to an international financial centre after China's Reform and Opening.
- Finally, as 1997 approached and Hong Kong prepared to return to Chinese sovereignty, we explored my uncle's decision to immigrate to Canada, and his thoughts and experiences as an immigrant.