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Performance of major stock markets

		30-Jun-11	% change		P/E Ratios on
		Index	YTD	in 2010	30-Jun-11
Hong Kong and Mainland					
Hong Kong	-HSI	22,398.1	-2.8%	5.3%	11.8
	-HSCEI	12,576.7	-0.9%	-0.8%	11.6
China	-Shanghai Comp	2,762.1	-1.6%	-14.3%	15.5
	-Shenzhen Comp	1,155.9	-10.5%	7.5%	30.4
Asia					
Japan	-Nikkei 225	9,816.1	-4.0%	-3.0%	18.0
Australia	-AOI	4,659.8	-3.9%	-0.7%	22.8
Taiwan	-TWSE	8,652.6	-3.6%	9.6%	15.3
Korea	-KOSPI	2,100.7	2.4%	21.9%	13.9
Singapore	-STI	3,120.4	-2.2%	10.1%	10.6
Thailand	-SET	1,041.5	0.8%	40.6%	13.3
Malaysia	-KLCI	1,579.1	4.0%	19.3%	16.8
Indonesia	-JCI	3,888.6	5.0%	46.1%	17.9
Philippines	-PCOMP	4,291.2	2.1%	37.6%	15.2
Vietnam	-VNINDEX	432.5	-10.8%	-2.0%	9.2
US					
US	-Dow	12,414.3	7.2%	11.0%	13.6
	-Nasdaq	2,773.5	4.5%	16.9%	23.5
	-S&P	1,320.6	5.0%	12.8%	15.0
Europe, PIIGS and Middle East					
UK	-FTSE100	5,945.7	0.8%	9.0%	14.2
Germany	-DAX	7,376.2	6.7%	16.1%	12.2

Asia

23. In Japan, the market was hit by a 9-magnitude earthquake in early March 2011. The subsequent tsunami and radiation leakages struck not only the country's economy but also stock markets worldwide. A stronger yen weighed on markets as well. To stabilise financial markets, the Bank of Japan injected liquidity into the banking system after the disasters. In addition, the Group of Seven intervened in the foreign exchange market to curb the yen's rally. Markets rebounded later as the nuclear crisis appeared to have stabilised. However, as long as the nuclear crisis remains unresolved, investors are likely to worry about its long-term

Southern China and the power shortage problem also had clouded the outlook on the Mainland’s economy.

Hong Kong

29. The Hong Kong markets rose initially on optimism over the economic outlook and solid

The European Sovereign Debt Problem

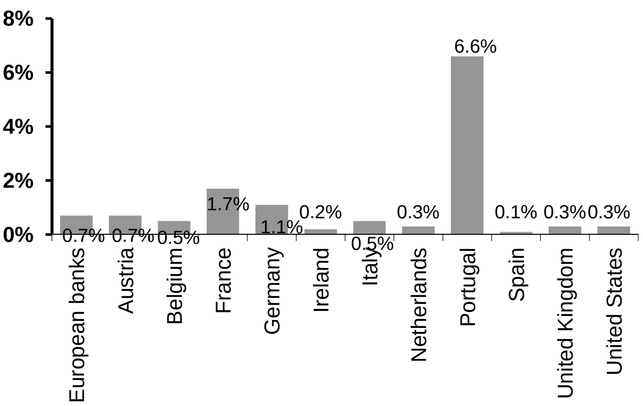
33. In 2010, the sovereign debt problem hit several European markets on heightened concerns over growing budget deficits and government debts. Market attention focused on the European countries collectively known as PIIGS.

34. In May 2010, eurozone finance ministers and the International Monetary Fund (IMF) announced a rescue fund to support these countries. The countries themselves also announced tightening measures aimed at reducing their fiscal deficits. Although the measures helped restore investor confidence in financial markets, some expressed concerns that they might hurt the growth prospects of the respective economies. There was resistance in implementing the measures.

35. Recently, the risks brought about by the European sovereign debt problem seem to have grown. In particular, concerns over the debt problem of bigger nations of Spain and Italy have grown. There are also concerns that the low interest rate environment may end soon, adding to pressure on debt-laden European economies. Also, the debt problem may affect political stability in some European countries, making it more difficult to resolve.

36. We have analysed the participation of major eurozone financial institutions in various segments of the Hong Kong securities markets. In the cash market, their combined share of the market turnover was about 12% in June 2011. In the derivatives market, they accounted for 6% of the trading in HSI futures and 9% of the trading in HSCEI futures. At this stage, there is no evidence to suggest that the sovereign debt problems have had a significant adverse impact on European financial institutions operating in Hong Kong.

37. In December 2010, claims of European banks on Greece amounted to 4.3% of their total foreign claims. However, the interdependence among certain countries in the eurozone can be significant. For instance, claims of French and German banks on Greece amounted to US$53 billion and US$34 billion respectively. The exposure of Portuguese banks to Greek debt accounted for 6.6% of its total foreign claims.



Banks' exposure to Greece (% of total claims) (December 2010)

Source: BIS Consolidated Bank Statistics

38. The direct impact of the European sovereign debt problem on the Hong Kong economy seems to be limited at this stage. However, uncertainty remains as to how the sovereign debt problems may impact the balance sheets or earnings of European financial institutions. If the problem affects the stability of European banks, it will affect the global economy and financial markets. Any downgrading of sovereigns and institutions by credit rating agencies may tighten credit market conditions and add to stock market and exchange rate volatility.

Major statistics of Hong Kong securities market (January – June 2011)

Volatility dropped in 2011

39. The intra-day volatility of the HSI dropped to an average of 1.1% from January to June 2011 (1.2% in 2010 and 2% in 2009). The implied volatility of the HSI options retreated steadily and was about 20% as at end-June 2011.

Intraday volatility of the HSI

Implied volatility of HSI options

Remark:

$$\text{Intraday Volatility} = \frac{\text{(Day High – Day Low)}}{0.5^{*}\text{(Day High + Day Low)}}$$

Source: Bloomberg

Trading activity in the local stock market

40. Trading activity in the local stock market was moderate during the first half of 2011. The average daily turnover amounted to $74 billion, about the same level as in the second half of sa.8(-)3.

Trading value of Hong Kong market ($ bn)

Trading volume of HSI constituent stocks (bn shares)

Source: Bloomberg

41. The trading hours of the local stock market have been extended from four hours to five hours

Short-selling activity

43. Short selling was active during the first half of 2011. Short selling rose in absolute terms and as a percentage of total market turnover from levels recorded in the second half of 2010. The average daily short selling was $4,964 million, or 6.8% of the total market turnover between January and June 2011, compared to $4,404 million or 6.9% in the first half of 2010 and $4,212 million or 5.7% in the second half of 2010.

IPO activity and performance

44. January to April 2011 was quiet for initial public offerings (IPOs) but activities have picked up since May. In the first half of 2011, there were a total of 29 IPOs (excluding Hui Xian REIT) on the Main Board, raising a total of $170.6 billion. This was more than the $50.2 billion raised in the first half of 2010, but less than the $398.6 billion raised in the second half of 2010.

45. The debut performance of these IPOs was mixed. The closing price of 16 of them rose, gaining between 0.3% to 65.9% on the first day of trading, while two closed flat and the remaining 11 suffered losses ranging between 0.3% to 23.2%. As at the end of June 2011, compared to their IPO prices, eight new stocks had risen, gaining 1.4% to 58.8%, one was flat and 20 recorded losses of between 0.2% to 53.8%.

Exchange-traded funds (ETFs)

46. The number of ETFs rose from 71 as at the end of 2010 to 76 as of 30 June 2011. In the first half of 2011, their average daily turnover was $2.4 billion, about the same level as in 2010. They accounted for 3.2% of the total market turnover, slightly less than its share of 3.5% in 2010.

Derivative warrants (DWs) and callable bull/bear contracts (CBBCs)

47. Trading of DWs was stable both in absolute terms and as a percentage of total market turnover in the first half 2011. Trading of DWs rose to $12.1 billion (16.5% of total market turnover), compared to $12.2 billion (16.5% of total market turnover) in the second half of 2010.

48. The trading of CBBCs decreased both in absolute terms and as a percentage of total market turnover. Trading of CBBCs decreased to $5.7 billion (7.8% of total market turnover), compared to $6.8 billion (9.1% of total market turnover) in the second half of 2010.