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**| RESEARCH ARTICLE**

## **Research on the Development Process and Prospects of Hong Kong, China's International Financial Center**

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**| ABSTRACT**

This article aims to delve into the development history and future prospects of Hong Kong, China's international financial center. Since opening up to the outside world for port construction, Hong Kong has leveraged its unique geographical location, historical background, and free economic system to rapidly develop its modern financial industry, gradually evolving into a globally renowned international financial center. The rise of a financial center to its current status is primarily attributed to two factors: the sophistication of economic and financial systems, and the pivotal turning points in industry development. While the initial accumulation of capital is crucial to the development of a financial center, Hong Kong's pre-colonial era was marked by a low level of social development and a small population, meaning that the initial accumulation of capital was relatively later-stage. Consequently, the impact of industrial transformation on Hong Kong's overall financial sector can be deemed negligible. This article primarily analyzes the reasons behind Hong Kong's secure position as an international financial center from three angles: its development history, current status, and future prospects, as well as the potential opportunities and challenges it may encounter.

**| KEYWORDS**

Hong Kong's modern financial industry, financial center, development history, current development status, development prospects, securities market.

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### **1. Introduction**

#### **1.1 Research Background**

Hong Kong's status as a financial center has been forged over the years through its close cooperation with the mainland in pursuit of shared prosperity. National support has bolstered its resilience against crises, fostering the vigorous growth of its financial industry. As a pivotal hub for offshore Renminbi (RMB) business, Hong Kong has accelerated the internationalization of the RMB. Interconnectivity mechanisms such as the "Stock Connect" have further consolidated its position as an international financial center. Hong Kong boasts a mature financial market, serving as a bridge between the mainland and the global economy and trade, with its banking sector exhibiting particular resilience, pointing to a promising future.

Hong Kong's significance in the global financial system lies in the continual enhancement of its financial center status, the robustness of its financial system, and the safeguarding provided by the "One Country, Two Systems" framework. Simultaneously, Hong Kong actively integrates itself into the overall development strategy of the country, strengthening its external economic ties and collectively shaping its uniqueness and global influence as an international financial center. With the implementation of national strategies such as the "14th Five-Year Plan," the Guangdong-Hong Kong-Macao Greater Bay Area development, and the "Belt and Road" Initiative (Li & Liu, 2023), Hong Kong is poised to embrace new development opportunities. The Hong Kong Special Administrative Region Government has also continually introduced new policies, including measures outlined in the "Chief

Executive's 2023 Policy Address," aimed at enhancing economic vitality, creating opportunities, and ensuring Hong Kong's long-term prosperity and stability.

## **1.2 Research Objectives**

This paper aims to comprehensively understand and analyze the evolution, current status, challenges faced, as well as future trends and potential of Hong Kong as an international financial center. Through this research, it seeks to facilitate interdisciplinary exchange and integration, providing a holistic and profound understanding of Hong Kong's international financial center status. Additionally, it aims to offer valuable insights and references to policymakers, financial institutions, and academia, thereby contributing to the sustainable development and enhancement of Hong Kong's financial industry's international competitiveness.

## **1.3 Literature Review**

### **1.3.1 Definition and Classification of International Financial Centers (IFCs)**

International Financial Centers (IFCs) typically refer to cities or regions that hold significant importance and influence within the global financial system. These areas boast highly developed financial markets, advanced financial infrastructure, and robust financial service capabilities, enabling them to provide a wide range of financial services and products to both domestic and international investors and financial institutions.

The classification criteria of IFCs can be examined from multiple dimensions, such as market size, the diversity of financial services, the concentration level of financial institutions, and the dynamism of financial innovation. Different classification standards may lead to variations in the understanding and evaluation of IFCs. The assessment of IFCs is often based on a series of indicator systems, reflecting their comprehensive strength and competitiveness. For instance, the Global Financial Centers Index (GFCI) encompasses five major indicators (Li & Hu, 2023) : business environment, financial system, infrastructure, human capital, reputation, and other comprehensive factors.

### **1.3.2 Comparative Study of Domestic and International Financial Centers: Contrasting Similarities and Differences between Hong Kong and London**

#### **Market Scale:**

- London boasts a large stock market, yet Hong Kong excels in liquidity;
- London's bond market is dominated by its local currency, while Hong Kong's comprises mostly non-local currencies;
- London's foreign exchange market is the largest globally, whereas Hong Kong leads in USD-CNY transactions;
- London's futures market is substantial, and Hong Kong's stock derivatives play a significant role.

#### **Financial Innovation Capability:**

- London excels in both traditional and innovative financial products;
- Hong Kong, on the other hand, rapidly develops in financial technology and green finance.

#### **Regulatory Environment:**

- London's regulatory system has undergone numerous reforms;
- Hong Kong's regulatory framework is robust and efficient.

#### **International Influence:**

- London, with its long history, wields profound influence globally;
- Hong Kong, as an emerging financial center, has seen its influence strengthen, particularly within Asia.

## **2. The Evolution of Hong Kong's International Financial Center**

The status of Hong Kong as an international financial center has undergone three significant stages of development: In the 1970s, Hong Kong seized the opportunity of Western financial globalization to open up its market, initially establishing itself as a regional financial center. During the 1990s, with China's financial reform and opening-up, Hong Kong achieved a transformation and upgrading of its financial center status, expanding into the international arena. At the beginning of the 21st century, riding on the wave of RMB internationalization, Hong Kong has further solidified its position.

Starting as a fishing village in the early 19th century, Hong Kong evolved through its transformation into an entrepot and free port after the Opium Wars, gradually becoming one of the global economic hubs. Since the mid-19th century, Hong Kong has attracted global resources, driving the prosperity of shipping, finance, and other industries. After World War II, Hong Kong emerged as a commercial and trade hub, navigating the challenges of declining entrepot trade through industrialization. Throughout this period, Hong Kong's financial markets have undergone numerous fluctuations and reforms, including the rise of the stock market, the introduction of banking regulations, banking crises, and financial liberalization.

Entering the 1970s, Hong Kong actively pursued a diversification strategy, fostering transformations in its industrial, market, and economic structures, with finance, real estate, and tourism flourishing. The establishment of the Stock Exchange of Hong Kong in 1980 marked a new era for the securities market, followed by the implementation of a free-floating exchange rate system and the linked exchange rate system, ensuring economic stability and growth.

With China's reform and opening-up, Hong Kong's economic ties with the mainland have become increasingly tight, gradually transforming Hong Kong into a service-oriented economy. After Hong Kong's return to China in 1997, it navigated the Asian Financial Crisis smoothly with the support of the Hong Kong Monetary Authority and the Central Government. In the 21st century, financial ties between Hong Kong and the mainland have deepened, with Hong Kong gradually establishing itself as an offshore RMB financial center and becoming one of the world's leading exchanges, further consolidating its status as a financial center.

Hong Kong's development journey has been filled with challenges and opportunities. Its transformation from a fishing village to an international metropolis not only showcases its remarkable economic leap but also embodies its unique political, economic, and cultural characteristics.

### **3. Current Status Analysis of Hong Kong as an International Financial Center**

#### **3.1 Overview of Financial Markets**

##### **3.1.1 Stock Market**

After reforms in 2024, Hong Kong's stock market experienced an upward trend, with IPO listings ranking among the top globally in the first half of the year. Driven by policies and international capital flows, the market witnessed enhanced liquidity and valuation. It is projected that the total IPO fundraising for the year could reach HK60billion to HK100billion, with notable performances from retail consumption and logistics sector enterprises. Market reforms such as the Stock Connect program have fostered positive expectations, resulting in diversified individual stock performances but an overall positive momentum and development potential.

##### **3.1.2 Bond Market**

Hong Kong's bond market remains robust, with sustainable bonds and dim sum bonds particularly standing out. The sustainable bond market has grown rapidly, led by government green bond issuances. The dim sum bond market has significantly expanded, and Bond Connect transactions remain active. The Special Administrative Region (SAR) government plans to expand bond issuance to consolidate Hong Kong's position as a green finance hub. The Hong Kong Monetary Authority (HKMA) has released a sustainable finance taxonomy, aligning with international standards. Hong Kong demonstrates leadership in the green bond market, facilitating capital flows and green transformation. In 2024, the bond market in Hong Kong will become more diversified and internationalized, strengthening its ties with mainland China and injecting new vitality into the market.

##### **3.1.3 Foreign Exchange Market**

As of the end of January 2024, Hong Kong's foreign exchange reserves slightly decreased to US\$423.2 billion (Fu, 2023), still equivalent to over five times the currency in circulation or approximately 40% of M3. In the first quarter, the Exchange Fund's investment income reached HK\$54.3 billion, with strong performance in bond investments and mixed results in equity and foreign exchange investments. Overall, this demonstrates the resilience and potential of Hong Kong's foreign exchange market.

##### **3.1.4 Gold Market**

At the beginning of 2024, gold prices surged, and Hong Kong's gold market became popular due to its low taxation and exchange rate advantages. The low-tax policy made gold prices more competitive for mainland China investors, while exchange rate fluctuations offered additional benefits. Looking ahead to 2024, gold is expected to remain popular, demonstrating resilience amidst global economic challenges, with central bank purchases pushing up prices. Inflation, trade tensions, and other factors may drive up commodity prices. Hong Kong's gold market is poised for strong growth, playing a pivotal role in the global market and maintaining its solid safe-haven status.

#### **3.2 Financial Institutions and Professional Talent**

##### **3.2.1 Types, Quantity, and Distribution of Financial Institutions in Hong Kong**

As an international financial center, Hong Kong boasts a unique financial institution system encompassing banks, foreign exchange, gold, and securities. There are three main categories: banking institutions, including numerous international bank headquarters with a significant foreign ownership share; non-bank financial institutions such as insurance companies, fund companies, trust companies, leasing companies, consulting firms, foreign exchange brokers, international gold traders, securities firms, investment advisors, and brokers; and a robust exchange and market infrastructure covering stocks, bonds, foreign exchange, and gold, with the Stock Exchange of Hong Kong Limited (SEHK) being a key financial hub in Asia. Hong Kong's financial institutions are densely concentrated, with Central as the core, followed by Kowloon, and strategic locations in the New Territories to cater to diverse needs.

### **3.2.2 Cultivation, Attraction, and Mobility of Financial Professionals in Hong Kong**

Hong Kong's financial hub boasts numerous educational institutions that nurture talent. The government has implemented talent strategies to address the growing demand for fintech and green finance professionals. The financial industry offers competitive salaries, attracting a large workforce with emerging professions. To address immigration trends, the government has relaunched investment migration programs and implemented Talent and Professional schemes to attract global financial talents. In Q1 2024, 2,735 individuals were approved under the Quality Migrant Admission Scheme, and 5,594 under Mainland Talent Introduction Plans. The financial industry employs over 270,000 people, with 100,000 working in banks, and annual job growth exceeding 5,000, indicating strong market demand.

### **3.3 Financial Regulatory System**

#### **3.3.1 The Supervisory Framework, Policies, and Implementation Effects of the Hong Kong Monetary Authority (HKMA):**

The HKMA oversees the banking system and safeguards financial stability in Hong Kong. In recent years, it has strengthened its supervision over cryptocurrencies, particularly stable coins, through collaboration with the government on legislative initiatives and engagement with the market and international counterparts. Furthermore, the HKMA fosters regulatory dialogue with the industry through its "sandbox" arrangements, thereby promoting financial innovation. To address operational risks, the HKMA issued the Supervisory Policy Manual (SPM) OR-2 in 2022, emphasizing operational resilience. This policy urges banks to enhance their capabilities in maintaining critical operations during disruptive events. Additionally, the HKMA revised SPM TM-G-2 on Continuity of Business Operations Planning and SPM OR-1 on Operational Risk Management to strengthen banks' preparedness for operational risk-related incidents. The implementation of these policies contributes to enhancing the overall robustness of the banking system.

#### **3.3.2 Strengths and Weaknesses of Hong Kong's Financial Regulatory System:**

- **Strengths:** As an international financial center, Hong Kong boasts a well-established system and strong attraction due to its mainland China connection. It possesses a solid financial foundation, numerous institutions, and a vibrant market. Its regulatory framework is transparent and efficient, with comprehensive data support.
- **Weaknesses:** Market volatility is heavily influenced by global factors, leading to intense competition and high talent mobility. The emerging trends in financial technology also pose regulatory challenges.

### **3.4 International Status and Influence**

Hong Kong's position as an international financial center remains solid, with high rankings in authoritative indices such as the Global Financial Centers Index (GFCI). Its geographical location, institutional setup, financial system, and talent pool contribute significantly to its role in the global financial architecture. According to the 2024 GFCI report, Hong Kong ranks fourth globally, behind New York, London, and Singapore. It also holds the third spot in the IFCI100, topping the list in Asia. Other reputable rankings also affirm Hong Kong's prominent financial position.

## **4. Challenges Facing Hong Kong as an International Financial Center**

### **4.1 Uncertainty in the Global Economic Environment**

In 2024, the global economic recovery remains sluggish, with increased vulnerability among financial institutions and high uncertainty in financial markets. Geopolitical tensions and a slow economic recovery pose threats to international financial stability. Hong Kong's banking sector faces both challenges and opportunities, needing to navigate credit risks, cross-border data issues, regulatory hurdles, and the emerging landscape of virtual assets, while leveraging the advantages of its status as a regional international financial center.

Global economic growth continues to rely heavily on Asia, particularly China, and Hong Kong's economic and financial stability is closely intertwined with that of the Asian region. While global inflation has moderated, it remains elevated, posing challenges to debt sustainability amidst high-interest rates. As a financial hub, Hong Kong must manage the implications of inflation and interest rate fluctuations.

### **4.2 Competitive Pressures from Domestic and International Financial Centers**

The 2024 Global Financial Centers Index (GFCI) indicates that Hong Kong, Shanghai, and Singapore rank prominently, with Singapore leading the Asian pack and posing competition for Hong Kong. Singapore, leveraging its Southeast Asian locational advantages and open financial policies, has gradually transcended the limitations of offshore business to expand globally. Shanghai, on the other hand, has actively pursued financial reforms and opened up its financial sector, becoming one of the cities with the highest concentration of global financial elements.

Competition is fierce among these three cities in the field of fintech. Hong Kong integrated concepts such as Web3.0 and the Metaverse into its Fintech Week in 2022, while Singapore focused on Web3.0 during its Fintech Festival in 2021. Hong Kong must strengthen its bridging role to counter the challenges posed by emerging financial centers.

## **5. Development Prospects and Strategic Suggestions for Hong Kong as an International Financial Center**

### **5.1 Development Prospects Forecast**

Hong Kong boasts unparalleled location advantages, a sophisticated and mature financial system, as well as the benefits of China's reform and opening-up era, all of which paint a bright future for its development. Over 4,000 headquarters and offices of major multinational corporations have been established in Hong Kong, and more than 600 fintech companies operate in the city, covering various emerging fields such as blockchain, payments, insurance Technology, and Regulatory Technology. These have generated massive international data flows for Hong Kong. Geographically, Hong Kong is situated at the heart of East Asia, with most major cities in the region accessible within a three-hour flight. Currently, East Asia has emerged as one of the most dynamic regions in the global economy, with rapidly growing financial demands. Secretary for Financial Services and the Treasury of Hong Kong, Mr. Stephen Hui, highlighted Hong Kong's unique strategic positioning as an international financial center, including its robust financial regulation and monetary system, its role as a buffer amidst global uncertainties, and its leverage in connecting the rapidly developing ASEAN and Belt and Road regions through its market.

A PwC survey revealed that Hong Kong's AI development is on par with major global financial centers, particularly in the application of AI in financial services. Challenges faced by Hong Kong in AI development include data availability and quality, cybersecurity, and data privacy. To facilitate AI's growth in the financial services sector, Hong Kong can implement necessary changes in its regulatory environment, such as establishing a robust data governance framework, regulatory sandboxes for testing and deploying AI technologies, and designated regulatory frameworks for responsible AI usage.

Hong Kong is also driving climate finance in the Asia-Pacific region to facilitate the transition to a low-carbon economy. The total amount of green and sustainable bonds issued in Hong Kong accounts for over one-third of the Asian market, and the city has implemented a common green taxonomy jointly developed by Mainland China and the European Union to facilitate cross-border climate capital flows.

### **5.2 Strategic Suggestions**

- Deepen interconnection with mainland financial markets and promote the internationalization of the Renminbi;
- Foster financial technology innovation to enhance service efficiency;
- Develop green and sustainable finance to build a shared investment system;
- Strengthen Hong Kong's position as a center for asset management and risk management;
- Expand financial cooperation with emerging markets;
- Address international economic changes to ensure market stability;
- Align with mainland regulations to promote financial market integration;
- Elevate financial service standards to attract international investment;
- Promote economic diversification and sustainability to enhance economic resilience.

## **6. Conclusion**

Hong Kong's economic development has continued to rise due to its advantages such as superior geographical location and international economic status. Its rise and development as an international financial center serve as a model of mutual achievement and win-win results between Hong Kong and the mainland (Shi, 2023). Hong Kong has undergone remarkable changes in the past few decades, especially in the increase of listed companies in new economic sectors, significantly enhancing the vitality and development potential of the Hong Kong market.

Hong Kong's internationalization, innovation, and cooperation are the key factors contributing to its status as an international financial center. The close cooperation between Hong Kong and mainland regulators and exchanges has been crucial to its development. Furthermore, Hong Kong has attracted a large number of new economic companies to list by implementing innovative regulatory measures and optimizing listing rules, further propelling the rapid development of the market. The future development of Hong Kong as an international financial center will focus on continuous innovation and cooperation.

Hong Kong will continue to leverage its unique geographical and cultural advantages, as well as its close ties with the mainland, to adapt to changes in the global economy and financial markets. Hong Kong's future development will emphasize new economies, green finance, and financial technology, while also strengthening its financial market interconnectivity with the mainland and enhancing financial cooperation with other countries and regions.

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