

THE HSBC GROUP: FROM KOWLOON TO KITCHENER

SPEECH BY

SIR WILLIAM PURVES

GROUP CHAIRMAN, HSBC HOLDINGS PLC

THE CANADIAN CLUB OF TORONTO/

HONG KONG - CANADA BUSINESS ASSOCIATION LUNCHEON

MONDAY, 15 APRIL, 1996

Madam Chairman, distinguished guests, ladies and gentlemen, it is a great honour for me to be here today. Your hospitality and your warm welcome are much appreciated. I do not get to Toronto often enough. The last significant visit was in 1992 when I was privileged to preside over the annual meeting of the International Monetary Conference which met for the first time in your beautiful city.

I am particularly honoured to be following in the footsteps of so many distinguished speakers -- I can but hope that, in this its 99th year, I can do justice to the proud traditions of the Canadian Club of Toronto and to those of the Hong Kong - Canada Business Association.

I have been asked to speak about the HSBC Group, one of the world's largest banking and financial services organisations, its origins in Asia and its role in modern-day Canada. But an occasion of this importance calls for more than a corporate history and I would like to take this opportunity to talk about wider developments in the world economy and how I see them affecting Canada.

But, before I do so, I am duty-bound to tell you a little about the HSBC Group whose name, is perhaps not as well-known in North America as elsewhere.

THE HSBC GROUP

The HSBC Group is an organisation founded in Asia in the last century and now privileged to have its own significant stake in Canada. As the title of my speech suggests, we have offices that stretch around the globe from Kowloon all the way to Kitchener.

It is no coincidence that both of these places were part of the British Empire for the origins of our Group lie in that great expansion of British trade and commerce that took place in the nineteenth century.

Yet what, besides this and some alliteration, have Kowloon and Kitchener in common?

Kowloon is a densely-populated peninsula on the South China coast whose name means "Nine Dragons". Kitchener was originally a German settlement -- called Berlin -- which turned patriotic in the First World War and changed its name to that of a well-known British General.

But, in fact, what links Kowloon and Kitchener is twofold. Firstly, the HSBC Group has operations in both places. And, secondly, as a result, both places symbolise the interdependence and interconnection of modern global business.

Kowloon and Kitchener may be geographically distant, but they are linked by the proprietary information technology and the global ownership structure of the HSBC Group. Kitchener is part of a network of 113 branches across Canada operated by Hongkong Bank of Canada, Canada's largest foreign-owned bank. HongkongBank, another of our subsidiaries, has more than 600 offices across the Asia-Pacific region including Kowloon.

Along with other subsidiary companies across Asia, the Middle East, Europe and the Americas, both banks report to a holding company headquartered in London.

This group of companies straddling East and West was originally established in 1865 as *The Hongkong and Shanghai Banking Corporation*. It was created by European, American and Indian merchants to finance trade between the South China coast and the rest of the world.

In the late-1950s, it began to form or acquire subsidiaries, and built up a "federation" of banks and financial services companies across the world -- a process which, from the Canadian perspective, culminated in the establishment of Hongkong Bank of Canada in Vancouver in 1981. This was subsequently consolidated through our acquisition of the Bank of British Columbia and Lloyds Bank Canada (formerly Continental Bank of Canada), as well as the Canadian businesses of Midland Bank, and the Australia and New Zealand Bank.

In Canada, as elsewhere, we believe that the local identity of the individual member company should come first -- a strong presence in a primary market. We give a large degree of autonomy to the local Board and management but expect them to deliver results. So, Hongkong Bank of Canada's President Bill Dalton and his predecessors, Jim Cleave and Gene Nesmith, were all Canadians -- a tradition we plan to continue.

Across your border, headquartered in Buffalo, we also own Marine Midland Bank and we are partners in a joint venture with Wells Fargo Bank, the *Wells Fargo HSBC Trade Bank*, an important supplier of international trade finance products and services to Californian companies.

This federated structure distinguishes us from other "global banks" -- such as Bank of America and Citicorp -- with their uniform worldwide presence.

In other words, the HSBC Group is an international federation of domestic banking franchises. Wherever we make serious money, we have a well-developed base of domestic retail customers. Canada is no exception.

We divide our business into five principal lines: commercial banking, investment banking, capital markets, insurance and general finance. But commercial banking accounts for over 90 per cent of our assets and profits.

Trade finance and other trade-related services are a long-standing core business. Our network in the Asia-Pacific region, Europe, the Americas and the Middle East is well-placed to finance the world's main trade flows.

The Group's global investment banking business, *HSBC Investment Banking*, is built on six major business streams: corporate advice, equity securities, project financing, private equity, asset management and private client services. In Canada, we provide most of these services from offices in Vancouver and Toronto.

Our international equity securities business -- *HSBC James Capel* -- is one of the oldest in Britain. Its research-driven institutional stockbroking operations are complemented by other securities-related activities such as derivatives trading, broking and advice, primary issue underwriting and corporate broking. In Canada, we have recently consolidated our ownership in HSBC James Capel Canada.

We have private banking operations worldwide and a global investment advisory and fund management business -- in the shape of *HSBC Asset Management* -- which currently manages funds in excess of CD\$45 billion. The recent purchase of MK Wong Associates in Vancouver brings in-house the firm that has been managing our very successful Canadian funds. That expertise is now available to our clients worldwide.

The Group's treasury and capital markets business ranks among the largest in the world, operating 24 hours a day and employing some 1400 dealers, with dealing rooms in 41 countries. Our Group's integrated dealing operations trade under the name of *HSBC Markets* while in our primary treasury centres of London, New York and Tokyo we operate as HSBC Midland.

As you can see we have a lot of different operations -- but what does this add up to in terms of financial muscle? Well at the end of 1995 our assets totalled CD\$481 billion and when the 1995 rankings are published we may well be number one in capital and profits and in terms of market capitalisation, we rank among the top 50 companies in the world. Size and capital strength is indeed important in our uncertain world but quality of service and reputational integrity are even more important.

The Group operates in more than 70 countries, has more than 3,000 offices and employs 100,000 people worldwide. We have close to 30 million customers.

Long-term, our strategy has been to create a strongly-capitalised international organisation with significant presences in Europe, the Americas, and Asia-Pacific. These are our main marketplaces, the three legs in what are sometimes described as our "three-legged stool". Canada is a significant part of that structure.

THE CANADIAN ECONOMY

So much for the trumpet-blowing for which I crave your indulgence. Now, let me tell you how we view the Canadian market.

As a Group, we are confident about prospects for the Canadian economy -- believing that the outlook for further interest rate cuts remains good and with potential for strong earnings growth on equity markets.

While we expect the momentum of recovery to continue, employment prospects remain a worry. But there are some glimmers of hope. Employment has picked up since the middle of last year at which time the economy looked in danger of slipping back into recession. Having said this I have to admit that, consumer spending shows little sign of strengthening in the short-term.

Overall, economic growth seems likely to be higher in Western Canada than in the Atlantic region, Quebec or the major industrial heartland of Ontario.

There are two long-standing challenges. Canada's public debt needs to be brought under control. It has increased by a factor of almost ten in the past two decades and around 40 per cent of the debt is owned by foreigners. The relentless rise in debt and the interest bill that comes with it, combined with a growing resistance to further tax increases, is now forcing a retrenchment in government spending. Paul Martin's determination to cut government spending is encouraging and deserves both domestic and international support.

We believe his recent Budget will be mildly deflationary in its impact. Most deficit targets will be met. But at the end of the present mandate, the Federal debt will still have increased by more than CD\$100 billion to well over CD\$ 700 billion, and the Federal government's share of GDP is likely to continue to rise at least through 1998-99.

However, the good news is that the budget deficit as a proportion of GDP is declining and according to Federal Government projections, will continue to decrease to around 2 per cent of GDP in 1997-98.

This is evidence that Canada understands the problem and is coming to terms with the excesses of the past.

For the time being, the Quebec referendum has settled the separatist issue. Lucien Bouchard has stated that he wishes to address the substantial fiscal problems of Quebec before returning to the question of separation and this must be welcome.

However, any perception of instability is always damaging, and I am sure international investors would like to see an early and permanent resolution of this long-running drama, one way or the other.

Generating economic growth must now be the primary consideration of all Canadians but, as ever, the performance of the United States will, to a large extent, determine Canada's success.

Canada has a reputation as a dynamic, open, international economy. In recent months, the Canadian Government has shown its determination to enhance that reputation still further with its Team Canada trade mission to south and south-east Asia.

Let us not forget that Canada has a vibrant, thriving Asian business community which is making a major contribution to the nation's economy as well as providing important links with Far Eastern markets.

CANADA AND ASIA

This business community as much as Asia itself will play a crucial part in Canada's future prosperity.

Presently, Asian gross domestic product (excluding Japan) represents around 40 per cent of combined European Union GDP, but recent estimates of trend rates of growth suggest that Asia is outstripping the West by as much as 4 to 5 times.

If this superior economic performance is sustained until 2010, it is expected that Asian GDP will then comfortably exceed that of the European Union. If we include Japan, over the same period it is conceivable that Asian GDP could exceed that of the European Union and the NAFTA countries combined. The implications for Canada are far-reaching. I suggest that Canada needs to turn its face more strongly towards Asia and strengthen its ties with that fast-growing region.

This is the backdrop against which the proposed European Union-Canada summit will take place in Italy in June. This summit will coincide with the G7 meeting in France, where Prime Minister Chretien is expected to sign a new transatlantic accord with European Union President Jacques Santer. But that will fall short of the NAFTA-European Free Trade pact that Mr Chretien proposed in a speech to the French National Assembly in December 1994.

Any interim agreement struck in June would certainly improve trade and investment ties, especially by dealing with troublesome non-tariff barriers. It would parallel the agreement between the US and the EU which was signed by the US President in Madrid last December.

Such negotiations confirm that Asia's challenge to the West is now very real indeed -- real enough to compel a response from European and North American governments alike. Asia is clearly beginning to influence the agenda.

Already the scale, both in absolute and relative terms, of Asian growth has led to an explosive growth in flows between North America and Asia -- in terms of goods and services, capital, people and companies, skills and ideas.

In 1994, monthly trade flows between North America and Asia (including Japan) were valued at more than USD40 billion. Canada is responsible for almost 14 per cent of that total but with Canadian GDP one tenth of that of the United States, this already suggests Canada is punching well above its weight.

In fifteen years' time, we can expect the value of such trade flows to treble. This may perhaps offer Canada an opportunity to diminish its dependence on the United States and to follow a path more like that of Australia which now looks more to Asia than to Europe and the Americas for its economic well-being.

Obviously, such flows will require financing -- global, competitive, trade services and treasury products will be critical to capturing the benefits of such growth.

The growth in trade flows will, however, pale into insignificance beside the growth in direct investment and investment in financial assets. We are all familiar with Asian (particularly Japanese) inward investment in North America but the trend is now beginning to balance out to a significant degree.

With the growth in purchasing power, Asian countries are ready markets for capital equipment and manufactured goods.

A recent study by the McKinsey Global Institute analysed, in great detail, the key drivers of international capital flows. It suggests that -- over the next ten years -- the emerging markets of Asia will receive a net inflow of capital of between USD600 billion and USD1 trillion.

By 2010, Asia could account for over three quarters of emerging market capital inflow, and a considerable proportion of this investment will emanate from the United States and Canada.

For the financial services sector, such flows will in turn generate banking business such as export and project finance, debt and equity issuance, securitisation, and fund management as well as growth in securities services and regional and global cash management.

This is an opportunity not just for a global group like HSBC but also for the Canadian financial sector as a whole and especially, for Canada's Asian business community.

POISED FOR SUCCESS

Looking westwards towards the Pacific and eastwards to Europe, Canada is well-placed to benefit from the flows of trade, capital, people and companies, skills and ideas.

The HSBC Group plans to benefit too -- our major strengths are our geographical and product footprint; the scale of our operations; our commitment to improved productivity; and our belief in long-term relationships. Hongkong Bank of Canada is an important part of that picture.

In 1865, the founders of the HongkongBank raised GBP400,000 in capital in Hong Kong. Their risk-taking has paid off. Over the past twenty-five years, share value has grown at a staggering 24 per cent compound rate. On only six occasions have we sought further capital from our shareholders and we continue to place our faith in the value of organic growth.

In recent times, we have seen some gloomy predictions for the return on equity for the banking industry as a whole. The HSBC Group does not share that pessimism. We believe that good sense will prevail and that the current quarrelling in parts of Asia will blow over and that Japan will surmount its present financial problems.

As the Asian economies continue to flourish over the next ten to fifteen years, trading between Asia and North America will offer some of the most exciting opportunities for major providers of goods and services.

The rise of Asia represents a challenge but more than that, it offers a golden opportunity -- probably the greatest opportunity we are likely to see in our lifetime.

Few countries are better-placed than Canada to benefit from Asian growth. Canada's geographic position, its low key political posture, its highly international economy, its rich blend of skills and resources and its large and growing Asian business community present a unique opportunity which I urge you to grasp.

At first glance, Kowloon and Kitchener may seem light years apart but as I hope I've shown today, nothing could be further from the truth. The two are drawing closer every day.