Dangerous Business Models: Bankers, Bureaucrats & Hong Kong's Economic Transformation, 1948-86

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Summary

Despite high-speed economic growth between 1948 and 1986, Hong Kong's banking industry displayed a marked propensity for self-destructive behaviour. The Government showed an equally strong tendency to ignore imprudent and illegal banking practices. As a result, major bank crises occurred in 1961-65 and 1982-86. This paper uses hitherto unpublished data and government archives to examine how banking behaviour responded both to economic development and the regulatory environment.

Hong Kong's banks made a crucial but largely unrecognised contribution to the creation of an export-manufacturing base in the 1950s. Bankers failed, however, to comprehend the economic transformation that was underway. The local Chinese banks tended to cling to outdated business models and did not modernise their management practices to match the growing scale and complexity of Hong Kong business. With some reluctance, foreign banks financed the industrial take-off.

The banking industry played a major role in Hong Kong's transition to a service economy and its emergence as a regional financial centre during the 1970s. Foreign bankers became more aggressive, and their management standards deteriorated. Local bankers stuck to their traditional business model, in which property speculation was perilously prominent.

Bankers' behaviour was shaped by official attitudes towards regulatory oversight and law enforcement. The Government deliberately created an environment in which the local Chinese bank group in particular was shielded from statutory and regulatory pressures to raise their standards. Bankers were able to ignore both banking and company legislation and to engage in criminal as well as imprudent practices with considerable impunity until 1964.

The Government facilitated a return to mismanagement and misconduct in the 1970s through its reluctance to regulate deposit-taking companies (DTCs). By enforcing an interest-rate cartel on licensed banks, the Government created a powerful inducement for these banks to set up their own DTCs. By refusing to grant more bank licences, it created a new class of banking outside the regulatory system because new entrants had to operate as DTCs.

Apart from a brief interval in 1965-70, therefore, the Government's consistent message to the banking industry throughout the period was of general indifference towards standards of behaviour so long as a serious bank collapse did not occur. The result was bank runs and bail-outs at considerable cost to Hong Kong's reserves.