

Record of discussion of meeting of Exchange Fund Advisory Committee Currency Board Sub-Committee held on January 17

The following is issued on behalf of the Hong Kong Monetary Authority:

(Approved for Issue by the Exchange Fund Advisory Committee on January 31)

Report on Currency Board Operations (October 9 – December 31, 2018)

The Sub-Committee noted that the Hong Kong dollar (HKD) exchange rate traded within a range of 7.8062 – 7.8459 against the US dollar (USD) during the review period. The HKD firmed against the USD since November, due to unwinding of interest carry positions as liquidity conditions tightened amid year-end funding demand. Towards the year-end, the HKD eased again, partly associated with repatriation of proceeds raised in initial public offerings, note-issuance activities ahead of holidays, and some re-building of interest carry positions. During the review period, the HKD interbank interest rates generally picked up, reflecting the expectation of US rate hikes and anticipated funding needs towards the year-end.

The Sub-Committee noted that the Aggregate Balance remained little changed during the review period. The Monetary Base increased to HK\$1,632.87 billion, mainly driven by an increase in the Certificates of Indebtedness.

The Sub-Committee further noted that, in accordance with the Currency Board principles, all changes in the Monetary Base had been fully matched by changes in foreign reserves.

The Report on Currency Board Operations for the period under review is at the Annex.

Monitoring of Risks and Vulnerabilities

The Sub-Committee noted that in the US, uncertainties over the monetary policy outlook and US-China trade tensions could point to heightened financial market volatility ahead.

The Sub-Committee noted that in Europe, economic policy and political uncertainties (e.g. Brexit) could aggravate the region's waning cyclical growth momentum to increase the risks of a sharper-than-expected economic slowdown.

The Sub-Committee noted that in Mainland China, the renminbi rebounded

following the US-China agreement to step back from additional tariffs. However, its growth momentum weakened and outlook became more uncertain.

The Sub-Committee noted that in Hong Kong, the economy slowed further in recent months amid heightened uncertainty stemming from the US-China trade tensions and the pace of US interest rate normalisation. The property market declined during the period and could face a number of headwinds in the near term.

An Event Study on the Linked Exchange Rate System (LERS) Operations

The Sub-Committee noted a study which investigated the effects of the triggering of the weak-side Convertibility Undertaking and the additional issuances of Exchange Fund Bills on the HKD exchange rate and interest rates. The study provided empirical support that the LERS had been functioning according to its design.