

Record of discussion of meeting of Exchange Fund Advisory Committee Currency Board Sub-Committee held on April 29

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

(Approved for Issue by the Exchange Fund Advisory Committee by Circulation)

Report on Currency Board Operations (January 1 – April 16, 2019)

The Sub-Committee noted that the Hong Kong dollar (HKD) exchange rate traded within a range of 7.8331 – 7.8500 against the US dollar (USD) during the review period. The interest rate gaps between the HKD and USD widened after the year-end mainly because of a drop in banks' funding demand. The widening of interest rate gaps attracted carry trade activities to sell HKD for USD, pushing the HKD towards the weak-side Convertibility Undertaking (CU). The weak-side CU was eventually triggered eight times in March. Reflecting the decrease in liquidity demand after the year-end, the HKD interbank interest rates generally declined, with short-dated interbank rates picking up after the triggering of the weak-side CU. The HKD strengthened in April due to the unwinding of carry trades as short-dated rates tightened. Overall, the HKD exchange and interbank markets continued to trade in a smooth and orderly manner.

The Sub-Committee noted that as a result of the triggering of the weak-side CU, the Aggregate Balance and the Monetary Base declined to HK\$54.3 billion and HK\$1,623.6 billion at the end of the review period respectively.

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 Annex.

Monitoring of Risks and Vulnerabilities

The Sub-Committee noted that in the US, equity markets responded favourably to the Federal Reserve's shift to a more dovish tone. However, the US Treasury yield curve remained very flat and briefly inverted in late March, highlighting heightened uncertainty over the economic outlook.

The Sub-Committee noted that in Europe, political uncertainties (e.g.

Brexit) and various external headwinds could prompt a more protracted deterioration in growth outlook.

The Sub-Committee noted that in Mainland China, while growth momentum remained lacklustre, signs of improvement had emerged.

The Sub-Committee noted that in Hong Kong, incoming data pointed to a slowdown in economic growth in early 2019, while the housing market saw increased transaction volume and accelerated price growth.

Understanding the Relationship between the Aggregate Balance and Interest Rates in Hong Kong

The Sub-Committee noted a study which provided qualitative and quantitative assessments on how the relationship between the Aggregate Balance and interest rates had evolved.