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**Seventh Issue  
(October 2005)**

The Institute was established by the Hong Kong Monetary Authority (HKMA) in August 1999 to conduct and support research on issues in monetary policy, banking and finance that are of strategic importance to Hong Kong and the Asian region.

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# Hong Kong Institute for Monetary Research -- *Newsletter*

## Remarks by the Director

A little over six months ago I took over from Stefan Gerlach as the Director of the Institute. I had been a visiting fellow before so I was already familiar with some of its activities. But it is only by being here over a longer period that one experiences the breadth of activities that the Institute supports. Thanks to Stefan, and before him Guy Meredith, the Institute has established itself as an important promoter and disseminator of research as well as a centre where policy makers and academic researchers meet to debate important issues in monetary policy and finance.

During the past six months we have organised a two-day workshop on 'The Property Market and the Mainland Economy', a three-day course on 'Structured Credit Products' intended for regional central bank officials, hosted eleven visiting fellows, issued fourteen Working Papers and one Occasional Paper, etc. You can find out more about these further on in this newsletter and on our web site.

At the time of writing, the near future looks equally exciting. In addition to holding the third HKIMR summer workshop in September we are co-sponsoring two international meetings with the Asian office of the BIS – a one-day workshop bringing together senior officials from central banks in the region to discuss monetary cooperation in East Asia under the chairmanship of Peter Kenen and a major international conference on 'Monetary Policy Approaches, and Implementation in Asia' which will gather academic and central bank experts and result in a comprehensive documentation of current practices and challenges for monetary authorities in the region.



*Hans Genberg  
Director of the Institute*

We are also continuing our collaboration with the Centre for Central Banking Studies of the Bank of England by offering a course for regional central bank staff on 'Financial Markets, Financial Stability, and Financial Fragility'.

Stefan Gerlach initiated a project to support research on the monetary history of Hong Kong. Working papers have already appeared and some Visiting Fellows are conducting research in the area. As you can see on page 3 of this newsletter, we are now uploading a newly-constructed data base containing historical statistics on the Hong Kong economy with the aim to encourage and facilitate further research.

These are but some of the activities that will take place during the remainder of this year. In addition we will have a full house of Visiting Fellows which implies many opportunities for informal discussions and seminars. This is why the Institute is such an asset to the Hong Kong Monetary Authority and Hong Kong more generally.

## Third HKIMR Workshop: Research on the Mainland Economy The Property Market and the Mainland Economy



*Xia Bin from State Council's  
Development Research Centre*



*Participants*

*The Institute organised a two-day workshop on “The Property Market and the Mainland Economy” on 11-12 July 2005.*

This was the third meeting in the Institute’s workshop series specifically related to research on Mainland China. This workshop was divided into three sessions with eight papers.

The first session focused on risks associated with property price developments in Mainland China. Xia Bin of the State Council’s Development Research Centre analysed risks and controls of the housing demand in Mainland China. Ping Xin Qiao of Peking University discussed the relationship between land prices and property prices while Jason Fang of Shanghai Fudan University presented a paper entitled “Is There a Property Bubble in Mainland China?”

The second session started with a paper on “The Property Market, Bank Lending and Macroeconomic Policy in China” by Zhang Tao of the People’s

Bank of China. Zhang Xiaojing of the Chinese Academy of Social Sciences then discussed property cycles and financial stability. This session ended with a paper presented by a director of the Institute, Peng Wensheng on a cross region study of the property market and the macroeconomy in Mainland China.

The last session introduced property market developments in other Asian economies. Zhu Haibin of the Bank for International Settlements presented a paper on “Housing Financing and Housing Prices: Some Cross Country Experiences”, while Masahiro Kawai and Wang Jingbin of the University of Tokyo discussed the reflections on the Japanese bubble of the 1980s.

Revised versions of the papers will be available on our web site.

## Financial Derivatives Course

Prof. Salih Neftci conducted a course on “Structured Credit Products: Market Examples, Risks and Pricing” at the Institute from 28 to 30 June 2005. The course consisted of five modules: the basic building blocks, correlation products, recent Credit Default Option structures, legal and regulatory aspects, and a detailed case study.

Around twenty participants from the Bangko Sentral ng Pilipinas, Bank Negara Malaysia, People’s Bank of China and HKMA attended the course. The course ended with a seafood dinner in Sai Kung.

Prof. Neftci of the City University of New York is an expert in financial engineering and shares his time between the academic and the investment sector. He is the author of two books entitled “An Introduction to the Mathematics of Pricing Financial Derivatives” and “Principles of Financial Engineering”. He has also lectured extensively to finance professionals and is currently a consultant with the International Monetary Fund. During two weeks in June 2005, he was a visiting Fellow of the Institute.



*Snapshot in front of the seafood restaurant  
in Sai Kung*

## Launch of the HKIMR Economic History Database

*The Institute has constructed a historical database, which is now available on the web site. It is open to the public and can be downloaded for research or educational purposes.*

### Objective

The database aims to encourage and facilitate research on the monetary and economic history of Hong Kong.

### Contents

The database contains a diverse range of economic and financial data that go back to as early as 1844. They cover currency in circulation, silver prices, exchange rates, bank deposits, public finance, land revenues, food prices, wholesale price index, retail price index, wage rates, merchandise trade with other countries, energy consumption, and other areas.

### Code Directory

Each data series is represented by a code. A code consists of three parts. The first part indicates the group to which a series belongs, e.g. “CUR” represents currency. The second part gives the distinctive feature of a series, e.g. “REV” represents revenue. The third part is the frequency code, e.g. “A” represents annual data. Underscores separate the three parts of a code. For easy reference, all the codes in the database are available in a document on our web site.

### Formats

The historical database is available in two formats: EViews and Excel.



### EViews

The database in the format of *EViews* consists of four component files. To facilitate the downloading of the data, the four files are stored in one zip file. Once the zip file has been downloaded, the user has to extract the four component files into one directory. Double-clicking the file “DB\_HKECONOMIC HISTORY\_EDB” opens the database.

### Excel Database

The database in Excel is comprised of worksheets. A worksheet stores the data series of a certain group. The name of a worksheet is the same as or an abbreviated form of the group’s name. Apart from the codes, information concerning the source, frequency, and period covered are also included. The worksheets are arranged alphabetically by their names.

We are interested in your feedback on this initiative. Please send your comments and inquiries to [hkimr@hkma.gov.hk](mailto:hkimr@hkma.gov.hk). We would also welcome being informed about research you may undertake using the data base as well as being acknowledged in such research.

## HKIMR Occasional Paper No.2

The Institute has published its second Occasional Paper entitled “Asian Monetary Union – Where Do We Go from Here?” written by Tony Latter.

The Occasional Paper series aims to disseminate non-technical policy-relevant analysis by prominent economists. The paper on “Asian Monetary Union – Where Do We Go from Here?” examines the various issues pertinent to the set up of a regional currency union for Asia.

Drawing on the experience of the European Monetary Union, it studies the general considerations of a monetary union, the conditions in Asia, the institutional and procedural aspects, and the preparatory work needed if an Asian Monetary Union is to be formed.

The full text and the summary of this paper are available on our web site.



## Visiting Fellow – Giorgio Valente



*Giorgio giving a seminar at the Institute*

The way I came across the Research Fellowship Program at the HKIMR followed a very ‘conventional’ route. In September 2003 I was invited to present a paper at the Eighth Australasian Macroeconomics Workshop locally co-organised by the Institute. During this event I had the opportunity to know more about its activity, its Research Fellowship Program and the wide range of scholars who have visited, or were visiting, the Institute. Then I decided to submit a research proposal, and I had the pleasure to visit the Institute two times, the first in July-August 2004 for five weeks and the second in August 2005, for five weeks.

During these visits I worked on two distinct research projects focusing on the behaviour of Hong Kong interest rates and their differentials with the US. In the first project I analyzed the impact of US monetary policy announcements on the term structure of Hong Kong (and Singapore) interest rate differentials. The questions I have tried to address are related to the intimate relationship linking the Hong Kong dollar to the US dollar by means of the fixed exchange rate arrangement. In fact, under the extant Currency Board mechanism, changes in US interest rates should be fully reflected in Hong Kong interest rates. However, the results of my empirical analysis (recently added to the HKIMR

*Dr. Valente of the University of Warwick visited the Institute for five weeks in August 2005 to undertake a research project entitled “The Microstructure of Interbank Liquidity and the Dynamics of Hong Kong Market Rates” with Joseph Fung and Shu-ki Tsang of the Hong Kong Baptist University*

working paper series) suggested a different picture, indicating long periods of time when interest rates in Hong Kong and the US were misaligned generating large (and surprisingly unexploited) arbitrage opportunities. During my first visit, I enjoyed the opportunity to share my thoughts regarding the Hong Kong interest rate market with other Research Fellows. These conversations led to the definition of a new research project, which is scheduled for completion by the end of August 2006. In this new adventure I and my two colleagues, Professors Joseph Fung and Shu-Ki Tsang of the Baptist University of Hong Kong, are currently investigating the reasons for the persistent differences between Hong Kong and US interest rates by exploring the microstructure of the Hong Kong interbank market.

When I first came to visit the Institute in July 2004, I was not new to Hong Kong since I had already visited the city a couple of times. If someone asks me to describe Hong Kong in few words, honestly there is little I can add to what has already been said. Nevertheless, my personal view is that although Hong Kong’s vibrant and dynamic environment is well known worldwide, its resulting mix of Chinese traditions and Western lifestyle is always a source of wonderment and interest. Surprisingly, despite the jet-lag and the tempting city’s amenities, I have noted (and this view is generally shared with many others Research Fellows) that, in both visits to the Institute, my research productivity did improve. I be-

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*“...although Hong Kong’s vibrant and dynamic environment is well known worldwide, its resulting mix of Chinese traditions and Western lifestyle is always a source of wonderments and interest.”*

*...to be continued on next page*

## Pacific Economic Review

### Special Section: Deflation and Macroeconomic Issues in Hong Kong

The Pacific Economic Review has published five papers, which were the result of research projects supported by or presented at seminars organised by the Institute. These papers are published in a special section of the Review in Volume 10 Number 2, in June 2005 and the titles are as follows:

“Wage-Price Dynamics and Deflation in Hong Kong” by *Hans Genberg and Laurent Pauwels*

“The Relationship between Consumption, Income and Wealth in Hong Kong” by *Joanne Cutler*

“Deflation in Hong Kong SAR” by *Philip Schellekens*

“An Open-Economy New Keynesian Phillips Curve: Evidence from Hong Kong” by *Hans Genberg and Laurent Pauwels*

“A Dynamic Factor Model of Economic Activity in Hong Kong” by *Stefan Gerlach and Matthew Yiu*

## Upcoming Activities

The Institute will co-organise a conference entitled “Monetary Policy Approaches and Implementation in Asia” with the Bank for International Settlements (Asian Office) on 21-22 November 2005.

The Institute and the Centre for Central Banking Studies (CCBS) of the Bank of England will conduct a three-day workshop on “Financial Markets, Financial Stability, and Financial Fragility” in Hong Kong from 29 November to 1 December 2005. Two workshops with CCBS were also organised in 2002 and 2004.



*Modelling Practise during the workshop in 2004*

## Visiting Fellow – Giorgio Valente

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lieve that the favorable time difference with Europe and the US (which allowed me to work without the pressure of normal departmental duties and working issues with co-authors overseas) may have played a role together with the possibility of having interesting and stimulating conversations with other Research Fellows and resident economists at the HKMA. Further, the efficiency, courtesy and respect of the staff members of the Institute (and the stunning view of Victoria Harbour from the 84<sup>th</sup> floor of the Two IFC building!) also helped to create a peaceful environment to develop and give concrete form to new

research ideas. Since then I have been recommending the Institute to my colleagues and I am very much confident that the international recognition of the Institute will keep on flying high in the years to come!

It may be because of these and other personal considerations that I have recently decided to leave Europe and relocate to Hong Kong for a couple of years. In fact, I will start a new appointment as Associate Professor of Finance at the Chinese University of Hong Kong in September 2005.

## Visiting Fellows in the Second Half of 2005

15 July – 30 August

**Joseph Fung** (Hong Kong Baptist University)

1–26 August

**Eric van Wincoop** (University of Virginia)

1–31 August

**Giorgio Valente** (University of Warwick)

29 August – 23 September

**Volker Nitsch** (Free University of Berlin)

5–30 September

**Paul Mizen** (Nottingham University)

5 September – 4 December

**Catherine Schenk** (Glasgow University)

3 October – 4 November

**Michael Devereux** (University of British Columbia)

1 October – 31 December

**Leo Goodstadt** (University of Dublin)

### Upcoming Seminars:

**7 October 2005** *The role of the effective exchange rate in monetary frameworks: options, operations and effects*, Már Gudmundsson (BIS)

**10 October 2005** *Vehicle Currency Blocs*, Michael Devereux (University of British Columbia)

**13 October 2005** *Inflation Targeting and Exchange Rate Pass-Through*, Alessandro Flamini (Graduate Institute of International Studies)

**27 October 2005** *A Sustainable Currency Regime for Hong Kong and the Mainland*, Lok-sang Ho (Lingnan University)

**23 November 2005** *The Macroeconomic Implications of Financial Globalization: A Reappraisal and Synthesis*, Eswar Prasad (IMF)

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## Recently Published HKIMR Working Papers

**No.18/2005** “Cross-Country Relative Price Volatility: Effects of Market Structure” by Yin-wong Cheung and Eiji Fujii

**No.17/2005** “The Impact of a More Stringent Listing Rule with Pre-listing Earnings Requirements on IPO Performance: Evidence from Hong Kong” by Wai-yan Cheng, Yan-leung Cheung and Yuen-ching Tse

**No.16/2005** “An Output Perspective on a Northeast Asia Currency Union” by Yin-wong Cheung and Jude Yuen

**No.15/2005** “Inflation in Mainland China - Modelling a Roller Coaster Ride” by Michael Funke

**No.14/2005** “Equity Valuation in Mainland China and Hong Kong: The Chinese A-H Share Premium” by Zhijun Zhao, Yue Ma and Yuhui Liu

**No.13/2005** “Crisis and Challenge: The Changing Role of the Hongkong & Shanghai Bank, 1950-2000” by Leo F. Goodstadt

**No.12/2005** “Empirical Exchange Rate Models of the Nineties: Are Any Fit to Survive?” by Yin-wong Cheung, Menzie D. Chinn and Antonio Garcia-Pascual

**No.11/2005** “Corporate Finance Under Low Interest Rates: Evidence from Hong Kong” by Paul Mizen and Cihan Yalcin