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**Thirteenth Issue
(July 2008)**

The HKIMR 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.

Highlights of this issue:

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Hong Kong Institute for Monetary Research -- *Newsletter*

Housewarming of the HKIMR

To celebrate the move into its new office on the 79th floor of Two International Finance Centre, the Institute organised a housewarming party on 17 January 2008. The activity was joined by Mr. Peter Pang (Deputy Chairman of the HKIMR), Mr. Hans Genberg (Director of the HKIMR), Mr. Robert McCauley (Chief Representative of the Asian Office of the Bank for International Settlements) and colleagues from various departments of the HKMA, including the Senior Executive's Office, Research Department, Corporate Services Department and External Department. The roast pig-cutting ceremony represented the hope for a promising future for the Institute.



Hans Genberg (left) and Peter Pang
(right) cutting the roast pig



Robert McCauley of the BIS (middle) and
Peter Pang of the HKIMR (left)



Guests from the BIS and the HKMA



Discussion during the housewarming: Anella
Munro (BIS), Li-gang Liu (BBVA) and
Michael Salemi (The University of North
Carolina) (From left to right)

HKIMR/BIS First Annual Workshop of Asian Research FMI Network

The HKIMR co-organised the inaugural workshop of the Asian Research FMI Network of the Bank for International Settlements (BIS) on 21 January 2008.

The workshop was divided into four sessions with two papers being presented in each session. The first session was chaired by Hans Genberg of the HKIMR. In this session, Laurence Fung of the HKMA presented his paper entitled “Assessing Financial Market Integration in Asia: Equity and Bond Markets” while Alicia Garcia-Herrero of the BBVA gave a presentation of her paper “Why is There So Little Regional Financial Integration in Asia?”

In the second session, Masamichi Kono and Mamiko Yokoi-Arai of the Financial Services Agency of Japan discussed their paper “Dissecting Regional Integration in Financial Services from the Competition Policy and Trade Policy Perspectives” and Jee Young Jung of the Bank of Korea demonstrated the challenges and development path to regional financial cooperation in Asia.



Speakers and discussants of the workshop



Eli Remolona (BIS)

After lunch, the third session began with the presentation of “Measuring Economic Integration: The Case of Asian Economies” given by Matthew S. Yiu of the HKIMR. After that, Chris Becker of the Reserve Bank of Australia discussed the volatility and persistence of capital flows.

In the last session, Narayan Chandra Pradhan of the Reserve Bank of India delivered a presentation on the topic “Financial Openness and Integration of India with South East Asian Countries: An Analytical Perspective” followed by the demonstration of an empirical analysis on the financial integration of India’s stock market with global and regional markets by Janak Raj of the Reserve Bank of India.

After the presentations, the workshop participants enjoyed a delicious dinner at a Chinese restaurant in Central, which marked the successful completion of this workshop.



Matthew Yiu (HKIMR)



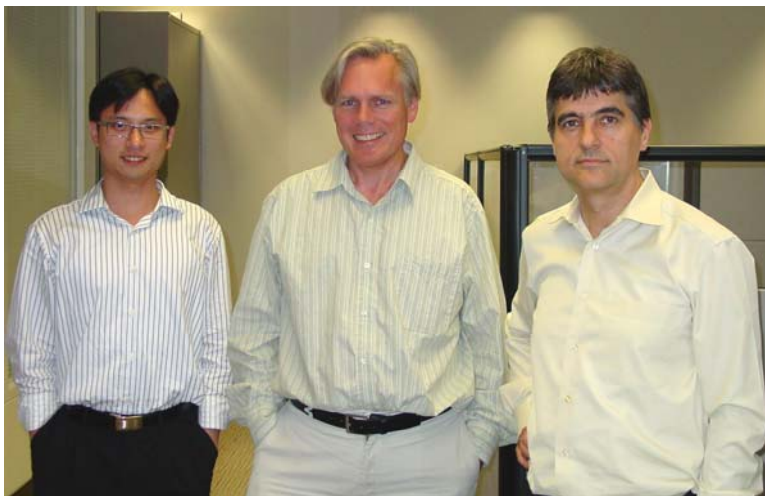
Participants enjoying the delicious Chinese dinner

Visiting Fellow – Philippe Bacchetta

Philippe Bacchetta is professor of macroeconomics at the University of Lausanne and a research fellow of the Centre for Economic Policy Research (CEPR, London). He received his Ph.D. and M.A. in economics from Harvard University and his B.A. and M.S. in economics from the University of Lausanne. From 1998 to 2007, Philippe Bacchetta was director of the Study Center Gerzensee, a foundation of the Swiss National Bank. He has also been an assistant professor at Brandeis University, USA, and at ESADE and the Instituto de Análisis Económico, both in Barcelona. He has also taught at the University of Geneva, the University of Freiburg (Germany), the Universitat Pompeu Fabra, the Universitat Autònoma of Barcelona, and CEMFI in Madrid. He has been visiting scholar at Harvard University, the IMF and the NBER and an academic consultant at various central banks. He is a fellow of the European Economic Association and an associate editor of the Journal of the European Economic Association. His research interests include open economy macroeconomics, international finance, and monetary economics.



The 79th floor of Two International Finance Centre, the location of the HKIMR, is a perfect place to observe the development of the Asian economies, in particular China. It is actually possible to see mainland China from the HKIMR on very clear days. Unfortunately, the number of clear days in Hong Kong appears to be decreasing and there was no very clear day during my stay. However, a large number of economists in the building study Asian economies. First, there are research fellows or visitors at the HKIMR. Second, there are economists working at the Hong Kong Monetary Authority, the BIS office, the IMF, or other private institutions. I learnt a lot from them at seminars or at other meetings. I was also pleased to recognise many faces that I had met in Gerzensee.



Alex Ho (Boston University), Eric van Wincoop (University of Virginia) and Philippe Bacchetta (University of Lausanne) (From left to right)

“The main reason for my visit to the HKIMR was to conduct a research project with my co-author, Eric van Wincoop. He had already visited the Institute on a couple of occasions and guaranteed that this was an excellent research environment. He was right and we had a very productive stay.”

But the main reason for my visit to the HKIMR was to conduct a research project with my co-author, Eric van Wincoop (University of Virginia). He had already visited the Institute on a couple of occasions and guaranteed that this was an excellent research environment. He was right and we had a very productive stay. We worked on a project on nominal exchange rate behavior. Our starting point is to consider an environment with model uncertainty. More precisely, the underlying parameters in the economy gradually vary over time, but are not observed by agents. We show that this uncertainty leads investors to vary the weights they attribute to various fundamentals in explaining exchange rate movements. This is consistent with the changes of focus typically observed in the foreign exchange market.

Using our model, we can examine the impact of parameter instability on forecasting performance. Meese and Rogoff (JIE, 1983) had shown that models based on fundamentals could not beat the random walk. A potential explanation that is proposed is precisely parameter instability. However, we show that this instability has little impact on forecasting performance. We feel that the small sample issue dominates most results found in the literature. There is still work to be done, both in the numerical simulations and in the empirical part. But, we made great progress on this project during the three weeks we overlapped at the HKIMR and I was able to present a seminar at the end of our stay. We hope to complete the project and write a paper in the next few months.

Conference on Global Liquidity and East Asian Economies

Together with the FRBSF Center for Pacific Basin Studies, Santa Cruz Center for International Economics, the University of Hong Kong and Lingnan University, the HKIMR co-organised a two-day conference on “Global Liquidity and East Asian Economies” on 26 and 27 June 2008.

Hans Genberg, Director of the HKIMR and the Executive Director of the Research Department of the HKMA, made opening remarks to commence the conference. A total of 13 papers were presented by speakers from various countries and organisations specialising in areas including determinants of international reserve accumulation, financial markets and the institutional environment, effects of financial liberalisation, capital controls, current account adjustment, empirics of exchange rates and FDI.

The event attracted over forty participants and generated lively discussions. The conference program can be found on http://www.hkimr.org/conferences_detail.asp?id=30&callfrom=previous&page=1



Hans Genberg (left) and Michael Hutchison (right)



Mark Spiegel (Federal Reserve Bank of San Francisco) presenting his paper.



Conference speakers and session chairs



Yin-wong Cheung (University of California, Santa Cruz and University of Hong Kong)

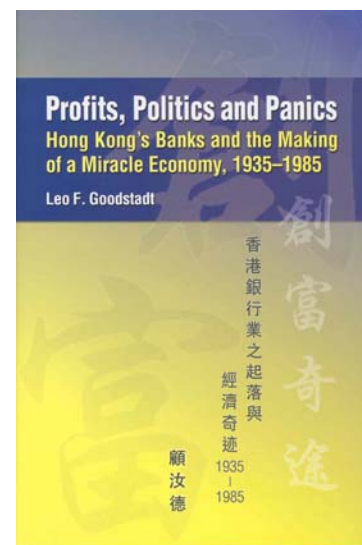


Jesus Seade (Lingnan University)

Fellows' Recent Books

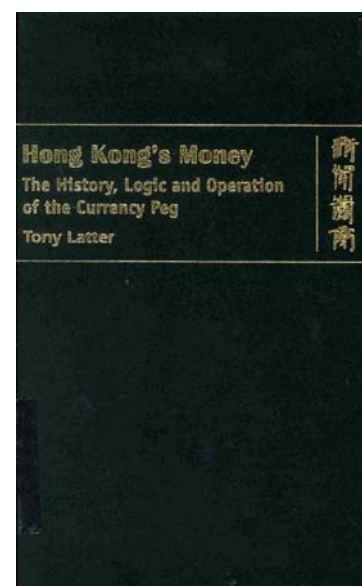
"Profits, Politics and Panics: Hong Kong's Banks and the Making of a Miracle Economy, 1935-1985" by Leo F. Goodstadt

"Profits, Politics and Panics: Hong Kong's Banks and the Making of a Miracle Economy, 1935-1985", written by Leo F. Goodstadt, was published in December 2007 by the Hong Kong University Press. This is the second of his three books reviewing the connections between government and business in Hong Kong. This new book examines the government's relations with banking and finance, a sector which played a crucial role in the creation of Hong Kong's economic 'miracle' between 1935 and 1985. It offers an absorbing account of a turbulent banking industry which will be compelling reading not only for bankers and corporate executives but also for readers interested in government's relations with business and the sources of Hong Kong's economic success. The four working papers which the author completed while he was a research fellow in the HKIMR are extensively cited in the book.



"Hong Kong's Money: The History, Logic and Operation of the Currency Peg" By Tony Latter

"Hong Kong's Money: The History, Logic and Operation of the Currency Peg", written by Tony Latter, was published in 2007 by the Hong Kong University Press. The book examines the introduction of Hong Kong's currency board in 1983, the development of China's currency system and how it affected Hong Kong. It also depicts the historical evolution of Hong Kong's monetary policy since the 1930s. In addition, the institutional structure of the HKMA and the Exchange Fund are discussed. This book draws extensively on his two HKIMR working papers, namely "Hong Kong's Exchange Rate Regimes in the Twentieth Century: The Story of Three Regime Changes" and "Rules Versus Discretion in Managing the Hong Kong Dollar, 1983-2006". Mr. Latter was a research fellow of the HKIMR in 2003, 2004, 2006 and 2008.



Upcoming Activities

4th Annual Central Bank Workshop on the Microstructure of Financial Markets

The Bank for International Settlements and the Hong Kong Institute for Monetary Research of the Hong Kong Monetary Authority are jointly organising a two-day workshop on the microstructure of financial markets, on 18 and 19 September 2008 in Hong Kong. This workshop will be the fourth in a series of similar events that have been held in Oslo (2005), Ottawa (2006) and Budapest (2007). It will provide an opportunity for researchers and practitioners to discuss theoretical and empirical issues regarding the microstructure of financial markets and for researchers studying different financial markets to interact.

Workshop on the Mainland Economy

The HKIMR and the Wang Yanan Institute for Studies in Economics (WISE) of the Xiamen University will co-organise a workshop relating to the Mainland economy on 16 and 17 October 2008. This is also the sixth workshop of the HKIMR workshop series relating to the Mainland economy. The theme of this workshop will be on China's financial market reforms.

Upcoming Visiting Fellows and Seminar

28 July – 30 September
Papa N'Diaye (International Monetary Fund)

4 – 30 August
Pierre Siklos (Wilfrid Laurier University)

18 – 29 August
Giorgio Valente (University of Leicester)

23 October – 18 December
Paul Mizen (University of Nottingham)

1 – 28 December
Ramkishan Rajan (George Mason University)

7 – 21 December
Kent Matthews (Cardiff University)

19 August 2008 *The Growth and Determinants of Vertical Trade in Korea* – Young Kyung Suh (Institute for Monetary and Economic Research of the Bank of Korea)

Deadline for Visiting Research Fellowship Applications

The Council of Advisors reviews proposals four times a year. The deadline for the next round of applications is *31 August 2008*.

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Recent HKIMR Working Papers

No.01/2008 *"The External Wealth of China: An Investigation from the International Balance Sheet Perspective"* by Andrew Sheng and Allen Ng

No.02/2008 *"Evaluating Foreign Exchange Market Intervention: Self-selection, Counterfactuals and Average Treatment Effects"* by Rasmus Fatum and Michael Hutchison

No.03/2008 *"Markets and Housing Finance"* by Veronica Warnock and Francis E. Warnock

No.04/2008 *"Assessing Credit Risk of Companies with Mean-Reverting Leverage Ratios"* by C. F. Lo, T. C. Wong, C. H. Hui and M. X. Huang

No.05/2008 *"Banking in China: Are New Tigers Supplanting the Mammoths?"* by Giovanni Ferri

No.06/2008 *"Too Much for Self-Insurance? Asian Foreign Reserves"* by Yuko Hashimoto

No.07/2008 *"Hoarding of International Reserves: A Comparison of the Asian and Latin American Experiences"* by Yin-wong Cheung and Hiro Ito

No.08/2008 *"Market Liquidity and FX Arbitrage in Emerging Markets: Evidence from Hong Kong Tick Data"* by Wai-Ming Fong, Giorgio Valente and Joseph Fung

No.09/2008 *"Stability Tests for Heterogeneous Panel Data"* by Felix Chan, Tommaso Mancini-Griffoli and Laurent L. Pauwels

No.10/2008 *"Input Substitution, Export Pricing, and Exchange Rate Policy"* by Kang Shi and Juanyi Xu

No.11/2008 *"Trends and Drivers of Bilateral FDI Flows in Developing Asia"* by Rabin Hattari and Ramkishan S. Rajan

No.12/2008 *"Environmental Factors Affecting Hong Kong Banking: A Post-Asian Financial Crisis Efficiency Analysis"* by Maximilian J. B. Hall, Karligash A. Kenjegalieva and Richard Simper

and more please visit our web site.