

**Second Issue
(January 2003)**

Welcome to the second issue of the Hong Kong Institute for Monetary Research (the Institute) Newsletter. Through it, we will provide you with information about recent and upcoming activities.

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.

Highlights of this issue:

Remarks by Mr. Stefan Gerlach, Director of the Institute.

Interviews with Professor Andrew Rose and Professor William Branson – visiting Research Fellows to the Institute.

Details of a joint workshop conducted by Bank of England staff, and of a HKIMR course on monetary economics designed and presented by Professor Carl Walsh.

Recent publications and activities of the Institute.

Hong Kong Institute for Monetary Research -- *Newsletter*

Remarks by the Director

Welcome to the Second Edition of our recently-launched twice yearly HKIMR Newsletter. The level of activity at the Institute continues to increase as it becomes better and more widely known. Our seminar series has remained very lively this Winter and we hosted a number of Visiting Research Fellows - including William Branson (Princeton) and Andrew Rose (UC Berkley) who are asked to share their thoughts and impressions of their stay in Hong Kong in this edition of the Newsletter. It is also encouraging that our links with Hong Kong's academic community are growing stronger, and that an increasing number of our visitors have

been asked to present their work at local universities.

Looking ahead, we have a full-year programme of events lined up including playing host to the 8th Annual Australasian Macro Workshop in April – our website gives details about how to submit papers for this and other forthcoming workshops and conferences. In addition, we would like to see more of you as speakers at our own seminars, so if you have any work that you would like to present please feel free to contact us.

Advisers of the Institute

To provide strategic guidance to the work in the Institute, we have a Council of Advisers, comprising internationally well-known scholars and prominent local academics and analysts. Presently, this has twenty members.

The overseas Advisers are: Charles Goodhart, David Hale, Ronald McKinnon, Guy Meredith, Alice Rivlin, Andrew Rose, Jeffrey Sachs, Eisuke Sakakibara and Glenn Stevens. As local Advisers, we have: Stephen Cheung, Tim Condon, Stefan Gerlach, Lok-sang Ho, Roger Luk, Simon Ogus, Wensheng Peng, Alan Siu, Kwong-yiu Tang, Shu-ki Tsang and Richard Wong.

The local Advisers meet every three months to discuss applications for the visiting fellowships in the Institute on the basis of written evaluations by local and overseas Advisers. They also participate in some of the Institute's work as speakers or discussants at conferences and seminars.

*Stefan Gerlach
Director of the HKIMR and
Executive Director of the Research
Department of HKMA*



*Guy Meredith (IMF),
one of the overseas Advisers,
giving a seminar at the Institute
in September 2002*

Visiting Fellow – Andrew Rose



Andrew Rose is the B.T. Rocca Jr. Professor of International Business in the Economic Analysis and Policy Group, Haas School of Business at the University of California, Berkeley. He is a Research Associate of the National Bureau of Economic Research.

Andrew first visited the HKIMR as a keynote speaker at a conference on Monetary and Financial Issues held in December 2001. He visited again last August to complete a paper on the potential benefits to a country's trade from joining a multilateral trade organisations, like the WTO and its predecessor the GATT (HKIMR Working Paper No.18/2002). He has recently agreed to become an overseas Adviser of the HKIMR.

Thanks for the opportunity to eat awesome dim-sum, Thai and Vietnamese.

In August 2002, I had the pleasure of visiting the Hong Kong Institute for Monetary Research for a second time. I came with my family for the rains of December 2001 (purported to be the optimal month), and was delighted to find the summer typhoons much overrated (with a nod to the sample size); the weather was spectacular for most of our three weeks. Miriam and Asher went to the beach on Cheung Chau Island for a week while I got to work hard; an agreeable situation for both sides! More recently my son has experienced the many joys of toddler-hood in Hong Kong (dim sum daily! Multi-level playgrounds! Ferries! The Peak Tram!) while I've enjoyed the peaceful environment of the office.

regression techniques. I find this negative result both mysterious and preposterous. No reasonable economist doubts that the GATT/WTO has had a substantial positive effect in liberalizing and encouraging trade over the last fifty years. But why can't you see it in the data? Chatting with skeptical colleagues, searching through the data and the World Wide Web for clues, and simply thinking hard in an empty office has clarified my views a lot. You might ask: what's the bottom line? Why doesn't the WTO seem to affect trade? I'm now *certain* both that I don't know and that it's an interesting mystery. Thanks to the Hong Kong Institute for Monetary Research for allowing me to advance to this stage – as well as the opportunity to eat awesome dim-sum, Thai, and Vietnamese!



Hard as it is to imagine, my time here has been even more productive than my week in December. I've been putting the finishing touches on a new paper concerning the (irr-) relevance of the multilateral system for international trade. In particular, I've found that the WTO and its predecessor the GATT seem to have a remarkably small footprint on trade. You basically can't see any impact on bilateral trade, once the usual "gravity" effects of GDP and distance have been accounted for through standard

My son has experienced the many joys of toddler-hood in Hong Kong



Andrew giving a seminar at the Institute

Visiting Fellow -- William Branson

William Branson is the John Foster Dulles Professor of International Affairs and Professor of Economics and International Affairs, in the Woodrow Wilson School of the Princeton University. He has served on the senior staff of the Council of Economic Advisers; as deputy director of OECD Project Interfutures; and as a consultant at the IMF and the World Bank.

Bill visited the HKIMR from late August through to early November 2002 to study exchange rate behaviour in South-East & East Asian economies and we are hoping to have him back later in 2003. Besides giving a seminar on his research results, he also gave a policy-oriented seminar on exchange rate arrangements in the Asian region.



In the fall of 2002, I enjoyed my first visit to the Hong Kong Institute for Monetary Research, although my first ever visit to HK was as an officer on a U.S. Navy ship in 1960! I was recruited by a letter from the director, Stefan Gerlach, whom I knew from his time at Brandeis, a pretty long ago. I came in the heat of late August, and will depart for now in the cooler weather of early November. When I came, I moved into the office just vacated by my old friend Assaf Razin. I found Andy Rose and Hans Genberg here, and Paul de Grauwe arrived shortly afterward. I also found at least three former students from a course in Beijing organized by my colleague Gregory Chow in 1985, now professors or senior researchers at HKMA.



A farewell party on Bill's last day at the HKIMR. Bill's wife, Elena (second from right), also visited the HKIMR and undertook a project on testing the TAR model and deviations from covered interest rate parity along the term structure of forward markets.

The Institute is incredibly friendly, convenient, and productive. I have been continuing my work here on cooperative exchange rate and monetary arrangements in groups of developing (or pretty thoroughly developed) economies, concentrating on Asia. The institute provides superb research help, in my case, my man Desmond Hou, who can provide data at the drop of a hat. I have also started a research project on price movements in HK and the Mainland with a former student now at the HKMA, Jimmy Ha.

I presented an internal seminar, a coffee-talk, in the Institute's language, on the SE Asian crisis as the bursting of a bubble in the market that relates the dynamics of the current account to the real exchange rate. This should appear as an Institute Working Paper. I also presented this in a seminar at the HK University of Science and Technology, far out in Eastern Kowloon. In addition, I had the opportunity to give a public policy talk on my research topic on Exchange Rate and Monetary Arrangements in Asia. This should appear as an Institute Occasional Paper, and I presented this at a seminar at HK City University, closer to home in Kowloon Tong.

I have greatly enjoyed travelling around HK, hitting restaurants in Shek O and Stanley market with old friends from the investment banking business. The restaurant scene here is awesome – any cuisine you can imagine. I took a day ferry trip to Macau, and I have been to Taipei to work with a former student there. He and I will journey to Xian to teach for a week when I leave. Thanks to the HKIMR for a productive and very enjoyable visit; I'll be back.

Thanks to the HKIMR for a productive and very enjoyable visit.

Workshop: Building Models for Monetary Policy in the Asian Pacific Region

The HKIMR and the Centre for Central Banking Studies (CCBS) of the Bank of England co-organized a workshop entitled “Building Models for Monetary Policy in the Asian Pacific Region” in Hong Kong from 8 - 12 July 2002.

The objective of the workshop was to learn how to build and use economic models that can be used to understand the monetary policy transmission mechanism. Lavan Mahadeva and Paul Robinson from CCBS conducted the workshop which was attended by over twenty representatives from the Bank of Thailand; Bank Indonesia; People's Bank of China; Monetary Authority of Singapore; Bank of Japan; Bangko Sentral ng Pilipinas; Bank Negara Malaysia; Bank of Korea; and the Hong Kong Monetary Authority.



Participants in the workshop



Day-tour for Lavan, Paul and participants on 13 July 2002

The two workshop directors, Lavan and Paul, gave lectures on the theory and use of econometric techniques for building models that can be used for the understanding and analysis of the monetary transmission mechanism. They provided advice to, and worked together with, workshop participants to help them construct their own small models that could be used to analyse monetary policy effects in their own economies. Towards the end of the workshop, each participant presented their small model and demonstrated how it could be used for forecasting and simulating monetary policy changes in their own economy.



The two workshop directors from CCBS: Lavan (right) and Paul (Left)



A seafood lunch on Lamma Island

After such an intensive workshop, on Saturday, the HKIMR organised an excursion for the participants and directors of the workshop. They visited Hong Kong's famous Stanley market before taking a boat trip to Lamma Island for a seafood lunch followed by a tour around Victoria Harbour.



Ashvin Ahuja (Bank of Thailand) presenting his small model of the Thailand economy

Course: Recent Developments in Monetary Economics and Policy



*Carl Wash
presenting the course*



*Chern Woon Lam
(Monetary Authority of Singapore)*



*Chang Shu
(Hong Kong Monetary Authority)*

The HKIMR organised a one week course entitled “Recent developments in Monetary Economics and Policy” in Hong Kong from 4 – 9 November 2002.

The course was designed and presented by Professor Carl Walsh of the University of California, Santa Cruz. It provided an update of developments in monetary economics over the past decade or so, drawing on material from Professor Walsh’s well-known book entitled ‘Monetary Theory and Policy’. The course was well attended by both HKMA economic staff and invited representatives from some of the world’s major central banks - including the People’s Bank of China; the Bank of Japan; and the European Central Bank.

The course focussed on New Keynesian macroeconomic theory and its implications for the design and conduct of monetary policy. This theory has spawned a rich literature directed towards building economic models that can be used for the understanding and analysis of monetary policy rules. A key advantage is that these models have firm microfoundations - based on assumed optimising behaviour by firms, households and central banks - that allows for a better understanding of the fundamental factors driving inflation. Professor Walsh reviewed much of this new literature and its implications for optimal monetary policy.

During the afternoon sessions, the course participants had the opportunity to present and discuss their own research at special seminars.

After a challenging and immensely rewarding week of study, the course participants enjoyed a harbour cruise and a seafood lunch at Sai Kung on Saturday afternoon organised by the Institute.



*A harbour cruise for
the course participants on
9 November 2002*



*Decymus (Bank Indonesia)
and Carl Walsh*

HKIMR Activities

The Institute hosted a workshop on deflation in Hong Kong and Asia on 5 June 2002. The aim of the workshop was to understand more about the current deflation in the region. Five speakers from the IMF, BIS Asian Office, HKMA and Lingnan University of Hong Kong presented studies. Twenty-eight participants attended the workshop.



*Philip Schellekens (IMF)
presenting his studies*

Recent Seminars:

30 October 2002 *Exchange rate and monetary arrangements in Asia*, William Branson (Princeton University)

17 October 2002 *Capital controls and exchange rate instability in developing economies*, Reuven Glick (Centre for Pacific Basin Monetary and Economics Studies)

15 October 2002 *Monetary policy in open economies under imperfect information*, Harris Dellas (University of Bern)

20 September 2002 *Surviving the slowdown: monitoring the European Central Bank 2002*, Paul De Grauwe (University of Leuven)

18 September 2002 *Escaping Japan's liquidity trap: an empirical assessment of the Svensson Proposal*, Guy Meredith (IMF)

5 September 2002 *The stochastic volatility model: an alternative to GARCH*, W.K. Li (University of Hong Kong)

Recently Published HKIMR Working Papers

Recent Working Papers:

No.21/2002 *Endogenous Exchange Rate Pass-Through when Nominal Prices are Set in Advance*, Michael Devereux, Charles Engel and Peter E. Storgaard

No.20/2002 *Signaling versus Commitment Strengthening: Exchange Rate Insurance against Currency Attacks*, Y. Stephen Chiu

No.19/2002 *Inflation Targeting in China?* Shu-ki Tsang

No.18/2002 *Do We Really Know that the WTO Increases Trade?* Andrew K. Rose

No.17/2002 *Foreign Exchange Exposure and Exchange Rate Arrangements in East Asia*, David Parsley and Helen Popper

No.16/2002 *Optimal Currency Area for Mainland China and Hong Kong? Empirical Test*, Shu-ki Tsang

No.15/2002 *From "One Country, Two Systems" to Monetary Integration?* Shu-ki Tsang

No.14/2002 *Hong Kong, Singapore and the East Asian Crisis: How Important were trade Spillovers?* Ramkishan S. Rajan, Rahul Sen and Reza Y. Siregar

and more please visit our web site.

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