

PILLAR OF STABILITY¹

Notwithstanding the worst financial turmoil in Asia, the monetary and banking systems of Hong Kong are holding up extremely well, and the financial markets are continuing to function efficiently. With other Asian currencies having depreciated sharply while the Hong Kong dollar has remained very stable, Hong Kong's competitive position has inevitably been affected and the painful economic adjustment has to continue. With the rule-based monetary system, prudent banking practices and robust financial infrastructure, however, Hong Kong will be able to cope and position itself for the recovery that will surely come. Hong Kong will be amongst the first in the region to recover and continue to be the pillar of stability in the region.

I understand that it is the tradition of the Dragon Boat Dinner that someone from Hong Kong should now speak on behalf of the guests. I am very honoured to have been asked to do so, for two reasons.

First, you have had very distinguished personalities such as Baroness Dunn, and the Chief Secretary of Hong Kong the Honourable Mrs. Anson Chan, performing this task on previous occasions. To be put in the same league, but perhaps not the gender, is of course a great honour.

Second, this is the first Dragon Boat Dinner after the Handover. The fact that, whether or not fortuitously, I am the chosen one from the Hong Kong Special Administrative Region to speak on this occasion is another great honour.

Ladies and Gentlemen, when Anson spoke at the last Dragon Boat Dinner before the Handover three years ago, she expressed confidence that the speakers of this evening would once again find cause to sing the praises of Hong Kong, this time, as a Special Administrative Region of China. Indeed she is right. And the cause is not difficult to find at all.

One can of course point to the smooth Handover itself, blessed so generously with the moving tears of the Goddess of Heaven, as Chinese

mythology has it, although I would rather have stayed dry.

Or one can point to the Annual Meetings of the World Bank and the International Monetary Fund of September last year, which were organized with the usual Hong Kong efficiency and have been recognized as the best ever.

But nothing is a better cause for singing the praises of Hong Kong than its sterling performance when the worst financial turmoil in the history of Asia swept through the region with such force.

Who would have thought that the Hong Kong Special Administrative Region, formed on 1 July 1997, could, one day after on 2 July 1997, be ready to brace the highly contagious turmoil, which broke out in Thailand and spread rapidly across the region and beyond?

Who would have thought that the Hong Kong Special Administrative Region could be the last and the least to be affected and be recognized as a pillar of stability, the eye of the storm or the typhoon shelter of Asia? Indeed, praises are called for.

And these praises should go first to a British Administration with foresight, working quietly and closely with the Chinese authorities over the years, meticulously preparing Hong Kong so it could cope

¹ This is the text of the speech by Joseph Yam, Chief Executive of Hong Kong Monetary Authority, at the 11th Dragon Boat Dinner in London on 2 June 1998.

with events of this nature, whether domestically generated or imposed upon it by external circumstances. This is a piece of history of the highly successful Sino-British cooperation that has gone unnoticed. But this was so by design in view of the market sensitivity of issues discussed and explored over a period of ten years ahead of the Handover.

I am very privileged to have been involved throughout this process - a process which contributed greatly to strengthening Hong Kong's monetary system, upgrading its supervisory standards and building a robust financial infrastructure. Indeed, the Hong Kong Monetary Authority, formed in 1993 and of which I also have the privilege to head from its beginning, is very much a part of that process. And so when the storm struck, the automatic stabilizers of a system that runs very much on its own were called into play and the worst currency attack since the establishment of the Hong Kong dollar's fixed exchange rate link with the US dollar subsided within two days.

Praises are also called for in the unwavering determination of the Hong Kong Government in continuing to manage the public finances of Hong Kong prudently and in continuing to run the Hong Kong economy through adherence to open and free market principles. This determination has enabled the stability of Hong Kong's currency to be underpinned and the credibility of Hong Kong's rule-based monetary system, which eschews interference for a political purpose, to be enhanced.

This is notwithstanding the greater involvement of an increasingly vocal community in public policy, encouraged by the gradual but significant process of democratization of Hong Kong, as clearly demonstrated in the very high turn out for the election nine days ago. We do have a community that behaves responsibly and capable of appreciating what is in the best interest of Hong Kong and what the alternatives may be.

Praises are further called for in the strict adherence by the Chinese authorities in Beijing to the terms of the Joint Declaration and the Basic Law. Almost a year now after the Handover, there has not been any departure from this position. The

Hong Kong Special Administrative Region has been enjoying the very high degree of autonomy that has been promised - a degree of autonomy, I should add, that is higher than that before the Handover. At least this has been my experience concerning matters under my areas of responsibility.

There are no more telegrams from the Foreign and Commonwealth Office (FCO) to read and respond "deskby", although I must confess that I do miss reading them. They were always very carefully drafted and opinions skillfully articulated. The phrase that I liked most was "seen from here", which was really the FCO at its best, used often when there was an alternative view for us, shall I say, to take into account in our deliberations. And to give weight to that view, every now and then there would be the subtle use of the personal pronoun "I" to signify that the telegram actually came from the Secretary of State himself, what we called an "I" telegram - something that required serious attention.

Yes we miss reading the masterpieces from the litterateurs of the FCO. But it is comforting that instead we have sincere and helpful expressions of confidence from Beijing in the ability of the Hong Kong Special Administrative Region to handle its own affairs and kind and forthcoming offers to help in case we need it.

You would have noticed what Mr. Zhu Rongji had said in his press conference on 19 March 1998 in Beijing after his appointment as Premier. He said that the Central People's Government had a high regard of the policies of the Hong Kong Special Administrative Region Government in dealing with the Asian currency crisis. He also said that the Central People's Government would spare no cost to maintain the prosperity and stability of the Hong Kong Special Administrative Region and to maintain the linked exchange rate system. Although this position had been known publicly for some time, for a Premier of the People's Republic of China to be so forcefully supportive provides quite a boost to confidence in Hong Kong under "one country, two systems".

Mind you, it is not so much the charisma of Premier Zhu that draws people's attention and convinces them that "one country, two systems"

works and is working well. It is more the act of leaving Hong Kong very much alone, for almost a year now after the Handover, which consolidates confidence in Hong Kong against very rough conditions in the Asian region.

It is also the success that China has had in continuing the process of reform and liberalization that instills confidence in the wider context. By unleashing market forces into the state-controlled sector, this process enabled substantial gains in productivity in the Mainland and created attractive opportunities to absorb redundancies from that sector. Notwithstanding the worst financial turmoil in Asia, the economy of the Mainland of China is forecast to grow by 8 percent in real terms this year. Inflation will be contained to below 3 percent.

And for the medium term there is the blue print of "one pledge, three targets and five reforms". These are not party slogans. They are tough but realistic measures for economic and social reforms in the Mainland of China, involving the cutting of bureaucracy, building markets and allowing market forces to play their proper role of effective resource allocation. And there is a high degree of confidence that the leadership will be able to deliver.

The reforms of China are not just of one man, but of a generation of technocrats and leaders who are pragmatic and alert to the prospects and the difficulties. There has been no denial of the complexity of the issues to be tackled and they know that the future of China depends on their success. All this augurs well for Hong Kong, for stability and prosperity in China will no doubt benefit Hong Kong immensely.

Ladies and gentlemen, in singing the praises of the Hong Kong Special Administrative Region, we should not, of course, overlook the tough challenges that we have to face. We should not overlook the need to continue to position ourselves in a manner that enables us to manage the inevitable crises and take full advantage of the associated opportunities.

Financial turmoil in Asia is an obvious challenge. With other Asian currencies having depreciated sharply while the Hong Kong dollar has

remained stable against the US dollar, which is itself quite strong, Hong Kong's competitive position has inevitably been affected. Indeed, economic growth in Hong Kong has been slowing down rather sharply since the middle of last year. For the first time since 1985, we recorded a negative growth rate in the first quarter of this year. And unemployment has been increasing. Asset prices have also fallen substantially, an inevitable adjustment having regard to the rather severe deflationary process the region is going through.

So there is pain all around. The innocent home mortgage payers and other borrowers are paying somewhat higher interest rates for their Hong Kong dollar loans, of about 200 basis points - an Asian premium that is remaining uncomfortably high. Many of them are also facing greater risks of losing their jobs. Indeed, the credit crunch is evident, and with economic conditions in Asia continuing to be unsettled, the situation may get worse before it gets better.

There may be further economic casualties, which may require modifications and improvements to government policies in such specific areas as securities regulation and housing. But I am pleased to say that the monetary and banking systems of Hong Kong are holding up extremely well, and our financial markets are continuing to function efficiently. Prudent banking practices in the past have provided an effective cushion for our banks, both in terms of capital adequacy and liquidity, to cope with this inevitable reversal of previous irrational exuberance. The Hong Kong dollar is furthermore not under any pressure. The robustness of the linked exchange rate system is now well understood, at least I hope by the speculators.

In this connection and in case there are residual doubts, a devaluation of the RMB is, at least to me, clearly not on the cards. With capital controls still in place and a balance of payments surplus in the Mainland, there is simply no pressure for the RMB to be devalued. Nobody can short the RMB. And the economic and political arguments are all for holding the exchange rate for the RMB stable, not just this year, or next, but for as long as the Mainland of China is serious about responsibly playing its part in the global trading and financial scene.

Meanwhile in Hong Kong, the painful but inevitable economic adjustment continues, and understandably there is discontent, and our democratically elected legislators are voicing this rather effectively. But it is clearly important that, as a responsible and caring government trying its best to ease the pain for the community in these difficult times, we should not lose our nerves and panic into doing things that would undermine the credibility of our well tested system. On issues of long term interest to Hong Kong, we must stick to our guns. And I have no doubt whatsoever that Hong Kong will be able to cope and position itself for the recovery that will surely come. I have no doubt also that Hong Kong will be amongst the first in the region to recover and will do so from a strong foundation.

Hong Kong's competitiveness is not all about costs and the exchange rate effects have in fact been exaggerated. With the traditional manufacturing sector having predominantly moved north of the border to the Mainland and with the services sector, in particular financial services, being now the mainstay of the economy, Hong Kong's competitive position, as an international financial centre, has been less sensitive to exchange rate changes.

The role of an international financial centre is to facilitate financial intermediation on an international dimension, channeling savings effectively and safely into investments, from those who have money to save to those needing money to invest in productive economic activity. That role is performed through the provision of financial markets in banking, debt and equity, and their derivative products.

With the substantial savings in the Asian region increasingly institutionalized through the creation of professionally managed provident funds, there has been an increasing emphasis on the need to manage the risks arising from such activities, particularly when they involve the movement of funds internationally and across currencies. There is increasing preference for operating in financial markets of established integrity, efficiency, transparency and liquidity. These are areas where Hong Kong, with free and deep markets operating under internationally accepted

standards, has a competitive advantage. These are areas where Hong Kong, with its modern and sophisticated financial architecture which is very much an integral and influential part of the global financial system, has much to offer.

By contrast, we have seen in the recent financial turmoil in Asia the meltdown of the financial systems of a few Asian economies, where financial markets have simply failed to function properly, seriously undermining confidence in these markets. So, notwithstanding relatively higher costs, I hope people, particularly institutional investors, are capable of looking at Hong Kong as a little different from the rest of Asia.

Beyond the current financial turmoil, there are of course further and arguably more important challenges for Hong Kong. Being the international financial centre in the most populated country in the world that is also sustaining strong economic growth and undergoing reform and liberalization presents many challenges for Hong Kong. Within the framework of "one country, two systems" and being prudent in the determination of our own policies, we will be able to meet these challenges. We will be able to benefit from the many opportunities and we will not forget the need to manage the inevitable risks that always come with prosperity.

There are also the challenges arising from progress in telecommunications and information technology. This is rapidly changing the global financial scene. With increasing popularity in smart cards and other forms of electronic money, and internet banking, there must be some doubt for the future of, for example, traditional branch banking with a large retail network. And what would be the role and form of an international financial centre when one can access, at the golfcourse at St. Andrews or on the beach of Phuket, financial markets across the world with just a computer notebook and a mobile phone? And how should the regulatory framework evolve to cope with all this? While we are all still scratching our heads and theorizing on what caused the current financial turmoil in Asia, and finding solutions for it, I fear that when the next one strikes, wherever this may occur, it may be of yet another kind that catches all of us by surprise. We must be prepared.

Ladies and Gentlemen, I am confident that, in the true Hong Kong style with which you all are familiar, the Hong Kong Administration and the Hong Kong people working together will be able to meet these challenges, just as we have done so in the past, and come through with flying colours. As you know, each rower of the dragon boat pulls his weight to the rhythm of the drummer in unison and the dragon boat speeds through the waves majestically. Hong Kong after the Handover has been through many choppy waves, some of them tidal in nature. Whatever the adversity, Hong Kong has come sailing through, and despite the turbulence, the Hong Kong Administration has been steadfast in objectives and decisive in action, and the Hong Kong people have been forthcoming in entrepreneurial spirit and austere in accepting the inevitable market adjustments. Ladies and Gentlemen, the drum of the dragon boat of Hong Kong continues to beat, not to the rhetoric of politics, but to the familiar rhythm of free and robust markets.

And on that note, may I, on behalf of the guests of this 11th Dragon Boat Dinner thank the hosts of this evening for their very generous hospitality. Thank you. 🍷