



Monetary Stability

Notwithstanding the uncertainties surrounding the future path of US monetary policy, global growth prospects, and geopolitical tensions, the Hong Kong dollar foreign exchange and money markets continued to trade in a smooth and orderly manner. The Hong Kong dollar exchange rate softened in the first four months of 2024 and then strengthened for the rest of the year. Under the Linked Exchange Rate System, the Hong Kong dollar interbank rates generally track their US dollar counterparts, while also being affected by local supply and demand. As the cornerstone of Hong Kong's monetary and financial stability, the Linked Exchange Rate System has shown its strength and resilience to various external shocks time after time.

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Objectives

The overriding objective of Hong Kong's monetary policy is currency stability. This is defined as a stable external exchange value of Hong Kong's currency, in terms of its exchange rate in the foreign exchange market against the US dollar, within a band of HK\$7.75–7.85 to US\$1. The structure of the monetary system is characterised by Currency Board arrangements, requiring the Monetary Base to be at least 100% backed by US dollar reserves held in the Exchange Fund, and changes in the Monetary Base to be 100% matched by corresponding changes in US dollar reserves.

The Monetary Base (Table 1) comprises:

- Certificates of Indebtedness, which provide full backing to the banknotes issued by the three note-issuing banks;
- Government-issued currency notes and coins in circulation;
- The Aggregate Balance, which is the sum of clearing account balances kept with the HKMA; and
- Exchange Fund Bills and Notes (EFBNs) issued by the HKMA on behalf of the Government.

Table 1 Monetary Base

| HK\$ million | 31 December 2024 | 31 December 2023 |
|--|---------------------|---------------------|
| Certificates of Indebtedness ^a | 601,415 | 592,585 |
| Government-issued currency notes and coins in circulation ^a | 13,047 | 12,927 |
| Balance of the banking system ^b | 44,802 | 44,950 |
| EFBNs issued ^c | 1,383,858 | 1,245,451 |
| Total | 2,043,122 | 1,895,913 |

- a. The Certificates of Indebtedness and the Government-issued currency notes and coins in circulation shown here are stated at Hong Kong dollar face values. The corresponding items shown in the balance sheet of the Exchange Fund in this *Annual Report* are in Hong Kong dollars equivalent to the US dollar amounts required for their redemption at the prevailing exchange rates on the reporting date. This arrangement is in accordance with the accounting principles generally accepted in Hong Kong.
- b. Balance of the banking system shown here is the carrying value before the amount advanced to the banks under the Discount Window Operations. In accordance with the accounting principles generally accepted in Hong Kong, the corresponding item shown in the balance sheet of the Exchange Fund in this *Annual Report* includes the amount of these advances.
- c. The amount of EFBNs shown here refers to their fair value. In accordance with the accounting principles generally accepted in Hong Kong, the EFBNs held by the HKMA on behalf of the Exchange Fund in relation to its trading of the EFBNs in the secondary market are offset against the EFBNs issued, and the net amount is recorded in the balance sheet. The EFBNs allotted on tender dates but not yet settled are included in the balance sheet but excluded from the Monetary Base. Therefore, the amount of EFBNs shown here is different from that in the balance sheet of the Exchange Fund in this *Annual Report*.

The stability of the Hong Kong dollar exchange rate is maintained through an automatic interest rate adjustment mechanism and the firm commitment by the HKMA to honour the Convertibility Undertakings (CUs). With the HKMA standing ready to sell (or buy) Hong Kong dollars to (or from) banks in exchange for US dollars upon request at HK\$7.75 (or HK\$7.85) per US dollar when the strong-side (or weak-side) CU is triggered, the Aggregate Balance will expand (or contract) to push down (or up) Hong Kong dollar interest rates, helping move the Hong Kong dollar back to within the Convertibility Zone of 7.75 to 7.85.

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Review of 2024

Exchange rate stability

The Hong Kong dollar moderated slightly in the first four months of 2024 amid softened liquidity. The Hong Kong dollar exchange rate strengthened between late April and mid-May, mainly supported by dividend-related funding demand and vibrant equity market activities. In early August, the Hong Kong dollar strengthened to the strong side of the Convertibility Zone amid short-lived concerns of a possible US recession and expectations of faster and deeper rate cuts by the US Federal Reserve that triggered an unwinding of carry trades and short Hong Kong dollar positions. Supported by a surge in local stock market activities following a series of economic stimulus measures announced in Mainland China, the Hong Kong dollar strengthened further in late September before moderating slightly in early November. The moderation was partly due to a pullback of the local stock market gains and partly due to the strong performance of the US economy at the time, which gave room for the Federal Open Market Committee to lower the federal funds rate carefully. Thereafter, the Hong Kong dollar rebounded amid seasonal year-end funding demand. Overall, the Hong Kong dollar exchange market continued to function normally throughout 2024 (Chart 1).

Chart 1

Market exchange rate in 2024



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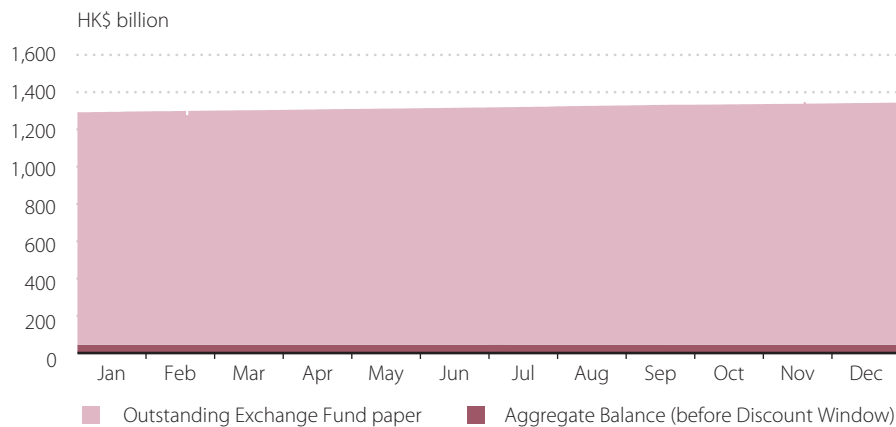
As the CUs were not triggered, the Aggregate Balance was little changed at around HK\$44.7 billion during the year. Meanwhile, the outstanding EFBNs increased slightly from HK\$1,245.5 billion to HK\$1,383.9 billion during the year. The total of the Aggregate Balance and outstanding EFBNs therefore increased from HK\$1,290.4 billion at the end of 2023 to HK\$1,428.7 billion at the end of 2024 (Chart 2). The Monetary Base as a whole remained fully backed by foreign exchange reserves.

HK\$1,428.7 billion

Total Aggregate Balance and outstanding EFBNs

Chart 2

Aggregate Balance (before Discount Window) and outstanding Exchange Fund papers in 2024



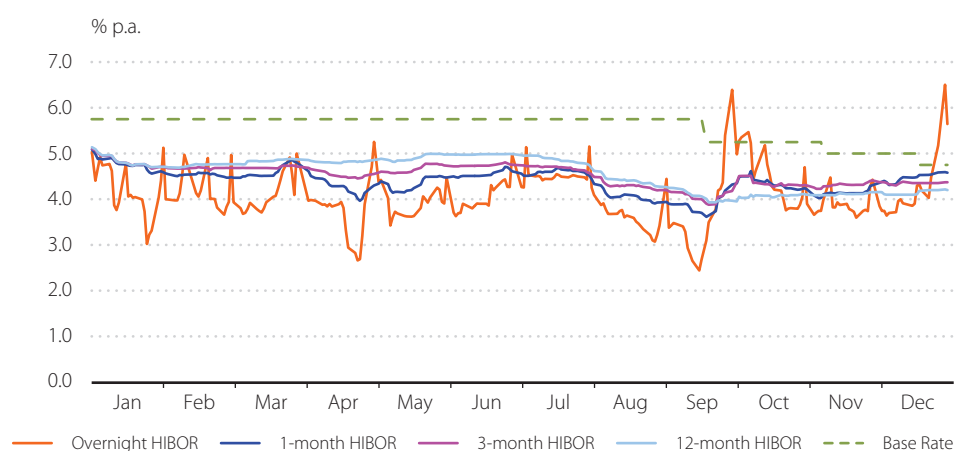
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Money market

Under the Linked Exchange Rate System (LERS), the Hong Kong dollar interbank rates generally track their US dollar counterparts, with the short-dated rates also responding to local supply and demand. The Hong Kong Interbank Offered Rates (HIBORs) generally softened in the first eight months of the year as the expectation of a US policy rate cut increased gradually (Chart 3). Driven by seasonal quarter-end funding demand and a buoyant equity market, HIBORs tightened in late September, with the overnight HIBOR once rising above 6% at the quarter-end¹. Thereafter, HIBORs remained largely stable before firming amid thinner liquidity ahead of the year end. For the year as a whole, the overnight, 1-month and 3-month HIBORs decreased by 45, 69 and 78 basis points respectively to 5.65%, 4.58% and 4.37% at year end.

Following the decreases in the target range for the US federal funds rate, the Base Rate was adjusted downwards three times by a total of one percentage point (i.e. 100 basis points) from 5.75% to 4.75% (Chart 3)². On the retail front, following the US policy rate cuts, many banks lowered their best lending rates by 25 basis points in mid-September, another 25 basis points in early November and 12.5 basis points in late December. Accordingly, the average interest rate of new mortgage loans declined from 4.13% in 2023 to 3.59% in December 2024. Overall, Hong Kong's money markets continued to function normally. Discount Window borrowing increased to HK\$50.0 billion in 2024 from HK\$38.8 billion in 2023 and no abnormality was noted in the relevant usage.

Chart 3 Hong Kong dollar interbank interest rates in 2024



¹ In view of the pickup of payment flows as the capital market turned vibrant, the HKMA temporarily extended the operating hours of Real-Time Gross Settlement systems for several days as a precautionary measure, allowing more time for banks to process payments and manage funding for client flows in late hours.

² The adjustments of the Base Rate were in accordance with the established formula, which sets the Base Rate at either 50 basis points above the lower bound of the prevailing target range for the US federal funds rate or the average of the five-day moving averages of the overnight and one-month HIBORs, whichever is the higher.

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The Linked Exchange Rate System

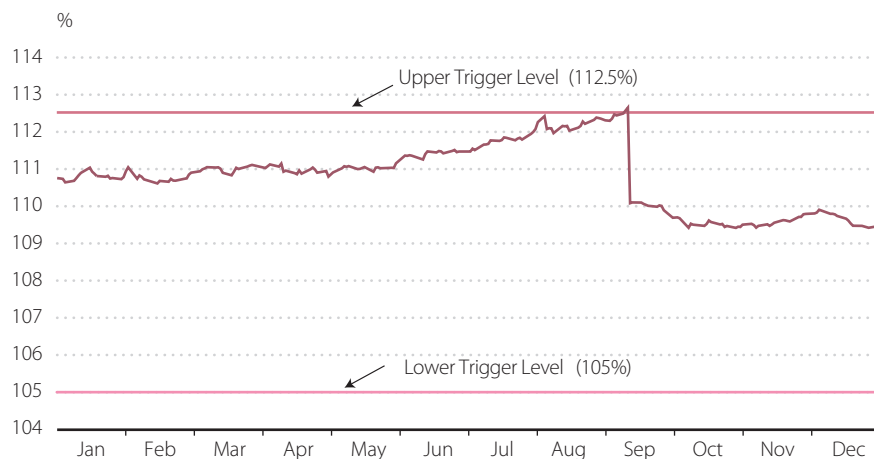
The LERS has served as a strong anchor of Hong Kong's financial system since 1983 and has shown its strength and resilience in the face of challenges. Despite uncertainties surrounding the future path of the US policy rate and geoeconomic fragmentation, the Hong Kong dollar exchange and money markets continued to function in an orderly manner, reflecting the robustness of the LERS.

The Government is firmly committed to the LERS. In its *2024 External Sector Report*, the International Monetary Fund (IMF) once again reiterated that the credibility of the LERS has been ensured by a transparent set of rules, large fiscal and foreign reserves, strong financial regulation and supervision, a flexible economy and a prudent fiscal framework.

A robust banking system is crucial to the normal functioning of the LERS. Hong Kong's banking sector continued to operate smoothly with liquidity positions and capitalisation faring very well by international standards. To ensure resilience of the banking sector, the HKMA has been closely monitoring banks' management of credit, liquidity and interest rate risks and stress-test results, and has maintained its supervisory efforts on bank lending.

To improve the transparency of the Currency Board Account, a specific portion of the Exchange Fund assets has been allocated to back the Monetary Base since October 1998. The Backing Ratio (defined as the Backing Assets divided by the Monetary Base) rose from 110.73% at the end of 2023 to a high of 112.65% on 10 September 2024, surpassing the Upper Trigger Level of 112.5% (Chart 4). The increase was mainly attributable to interest from investments and mark-to-market revaluation of investments. In accordance with the arrangement approved by the Exchange Fund Advisory Committee (EFAC), assets were transferred out of the Backing Portfolio to the Investment Portfolio to reduce the Backing Ratio to around 110.08% on 11 September. Thereafter, the Backing Ratio remained largely stable, ending the year at 109.56% on 31 December. Under the LERS, while specific Exchange Fund assets have been designated for the Backing Portfolio, all Exchange Fund assets are available to support the Hong Kong dollar exchange rate. The ample financial resources of the Exchange Fund, together with the sound banking system, provide a powerful backstop to Hong Kong's monetary and financial stability.

Chart 4 Daily movement of the Backing Ratio in 2024



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Currency Board Sub-Committee

The Currency Board Sub-Committee (CBC) of EFAC monitors and reviews issues relevant to monetary and financial stability in Hong Kong. In 2024, the CBC considered issues including the Hong Kong banking sector's exposures to non-bank financial institutions and the latest monetary policy implementation framework in major advanced economies. Records of the CBC's discussions on these issues and reports on Currency Board operations submitted to the CBC are published on the HKMA website.



Notes and coins

The value of the notes and coins in circulation at the end of 2024 is summarised below:



Total value of banknotes issued by note-issuing banks (Charts 5, 6 and 7)

HK\$601.4 billion

up 1.5% year on year



Total value of notes and coins issued by Government (Charts 8 and 9)

HK\$12.8 billion

up 0.9% year on year

Of which:

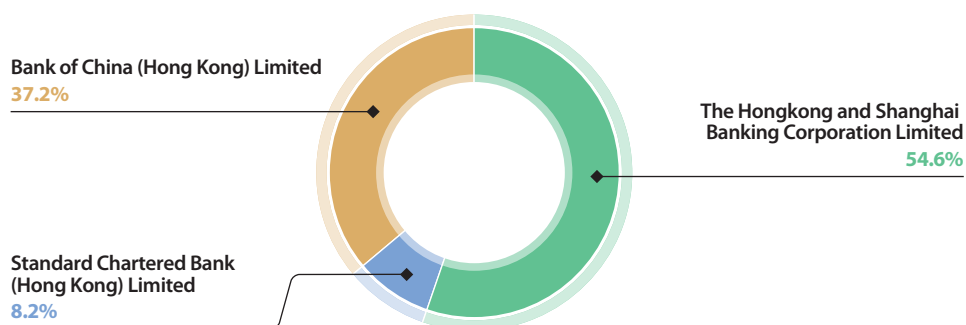
– Total value of HK\$10 notes

HK\$4.6 billion

83% were polymer notes

Chart 5

Banknotes in circulation by note-issuing banks at the end of 2024



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Chart 6 Distribution of banknotes in circulation at the end of 2024



Chart 7 Banknotes in circulation at the end of 2024

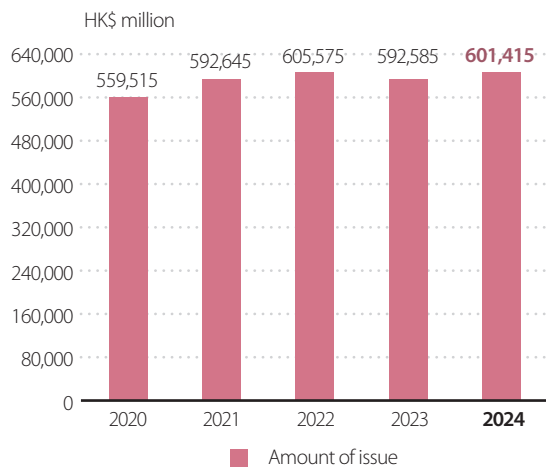
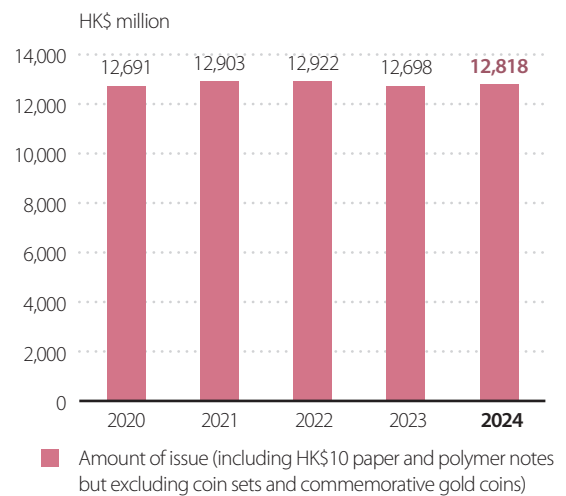
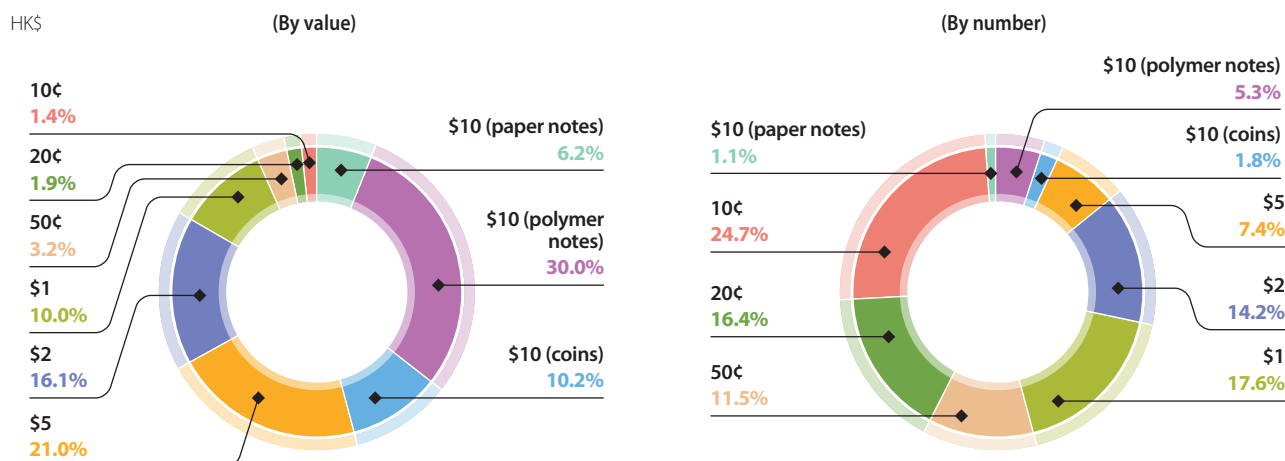


Chart 8 Government-issued currency notes and coins in circulation at the end of 2024



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Chart 9 Breakdown of Government-issued currency notes and coins in circulation at the end of 2024



Hong Kong banknotes

During the year, the HKMA organised 14 seminars on the design and security features of Hong Kong banknotes for more than 2,600 participants, including bank tellers, cashiers from retail establishments and students, to help enhance their knowledge and skills in authenticating banknotes.

Coin Collection Programme

The Coin Collection Programme continued to be well received by the public. More information about the Programme can be found in the *Sustainable HKMA* chapter of our *Sustainability Report 2024*.

US Dollar Liquidity Facility

The HKMA introduced refinements of the US Dollar Liquidity Facility, including shortening its settlement process from T+1 to T+0, with effect from 24 May. This standing facility provides licensed banks with backstop liquidity in case of need, particularly given the introduction of a shortened settlement cycle to T+1 in the US starting from 28 May.

Exchange Fund Bills and Notes

The EFBN Programme continued to operate smoothly. At the end of 2024, the nominal amount of outstanding Exchange Fund papers stood at around HK\$1,306.8 billion (Table 2).

Table 2 Outstanding issues of EFBNs

| HK\$ million | 2024 | 2023 |
|---|------------------|-----------|
| Exchange Fund Bills (by original maturity) | | |
| 28 days | 800 | 2,800 |
| 91 days | 819,650 | 775,680 |
| 182 days | 414,600 | 405,800 |
| 364 days | 56,100 | 52,700 |
| Subtotal | 1,291,150 | 1,236,980 |
| Exchange Fund Notes (by remaining tenor) | | |
| 1 year or less | 6,000 | 7,600 |
| More than 1 year and up to 3 years | 7,200 | 7,200 |
| More than 3 years and up to 5 years | 2,400 | 2,400 |
| More than 5 years and up to 10 years | 0 | 1,200 |
| Subtotal | 15,600 | 18,400 |
| Total | 1,306,750 | 1,255,380 |

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Monetary research

In 2024, the Hong Kong Institute for Monetary and Financial Research (HKIMR), the research arm of the Hong Kong Academy of Finance (AoF)³, released 15 working papers on monetary and financial research topics that are strategically important to Hong Kong and the region. The research findings were disseminated to a global audience through five issues of an open-access electronic journal. Additionally, two issues of *Insights from Monetary Research* were released to provide the public with a high-level non-technical summary of the HKIMR's recent research outputs.

Apart from its research activities, the HKIMR organised a series of knowledge exchange events to foster engagement with various participants. Aimed at local audiences, 31 seminars/webinars on important monetary and financial research topics were held during the year. On the international front, four international conferences and five seminars/roundtables were organised by the AoF and the HKIMR in collaboration with academic institutions, central banks and international financial institutions to promote dialogue and exchange on broader economic and financial issues.

These international events included the following:

11
Apr

International Conference on Central Bank Digital Currencies and Payment Systems

co-organised with the HKMA and the Hong Kong University of Science and Technology (HKUST)



6-7
Jun

NBER East Asian Seminar on Economics 2024

co-organised with the National Bureau of Economic Research, the Bank for International Settlements (BIS) and the Business School of the HKUST

15-16
Jul

Conference on Safeguarding Global Financial Stability in a New Era

co-organised with the IMF, the BIS and the ASEAN+3 Macroeconomic Research Office

14-15
Oct

The 14th Annual International Conference on the Chinese Economy — *China and the Changing Global Trade Landscape: Challenges and Opportunities*



³ The HKIMR is a subsidiary of the AoF.