

EDITORIAL

Recent trends and events

Growth of the Hong Kong economy remained solid in the fourth quarter of 2006, although the quarter-on-quarter growth rate had moderated to 1.3% from 2.6% in the third quarter. The slowdown is attributable to a decline in net exports and in business expenditure growth. Consumer price inflation picked up gradually in the quarter because of larger increases in food prices and higher residential rents. The unemployment rate fell to a six-year low of 4.4% in the quarter thanks to solid expansion of domestic demand and business activities.

The US federal funds target rate remained at 5.25%, and the local Base Rate at 6.75%, during the quarter. The Aggregate Balance was steady at around HK\$1.3 billion. Volatility in Hong Kong's equity market has increased since the end of 2006. The Hang Seng Index went as high as 20,830 on 22 February 2007, before falling to 18,659 on 5 March. It closed at 19,135 on 9 March.

The HKMA announced on 1 December 2006 the completion of the legislative procedure required to bring into effect the Banking (Capital) Rules and the Banking (Disclosure) Rules on 1 January 2007. These Rules prescribe how the capital adequacy ratio (CAR) of locally incorporated authorized institutions shall be calculated and what information on the state of affairs, profit and loss and CAR shall be publicly disclosed by authorized institutions. On 14 December, the HKMA and eight credit and debit card scheme operators in Hong Kong launched a *Code of Practice for Payment Card Scheme Operators*. On the following day, the HKMA launched two league tables of market makers for the Exchange Fund Bills and Notes (EFBN) to encourage trading activities in the EFBN market. On 16 January 2007, Joseph Yam, Chief Executive of the HKMA, and Zhou Xiaochuan, Governor of the People's Bank of China, signed a supplementary memorandum of co-operation regarding the issuance by Mainland financial institutions of renminbi-denominated bonds in Hong Kong. On 18 January, the HKMA announced the position of the Exchange Fund at the end of 2006. Following problems experienced with add-value transactions for Octopus cards involving EPS, the HKMA announced on 16 February that the Monetary Authority (MA), after consultation with the Financial Secretary, had appointed an Advisor under section 52(1)B of the Banking Ordinance to advise on the management of the Octopus Cards Limited (OCL). OCL was also required to submit to the MA an independent auditor's report on the operation of add-value services through EPS and OCL's operational risk control environment.

In a speech delivered at the High-Level Meeting on the Implementation of Basel II in Asia and Other Regional Supervisory Priorities on 11 December 2006, Joseph Yam spoke on the key challenges for macroprudential surveillance faced by central bankers and the ways to tackle them. He also called on the Executives' Meeting of East Asia-Pacific Central Banks (EMEAP) to work together with the international supervisory community to address these issues.

In this issue

This issue of the Quarterly Bulletin contains three feature articles. The first feature article is an annual review of Hong Kong dollar debt market development. The second is an assessment of the euro payment system in Hong Kong against the *10 Core Principles for Systemically Important Payment Systems* issued by the Bank for International Settlements. The third is a research article on Hong Kong's trade patterns and trade elasticities, which concludes that a real depreciation of the Hong Kong dollar would likely improve Hong Kong's balance of trade in direct exports and imports.