$1 billion injected to save US dollar peg

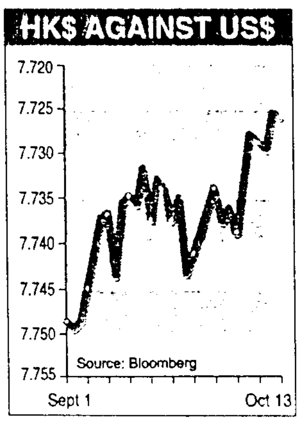
By NOEL FUNG

A BILLION dollar of government money has been pumped into the territory's banking system in an unprecedented move to hold down the value of the Hong Kong dollar.

The huge injection is the biggest of its type this year and follows almost two weeks of historic trading on the Hong Kong stock market in which local stocks have rocketed by almost 11 per cent in 11 days.

A massive influx of money from overseas investors, especially from the United States, had put the dollar under pressure to move up against the US dollar, the Government said.

The authorities are trying to stop the dollar strengthening as overseas demand for the local currency rises. Outside investors need to buy billions of Hong Kong dollars to enable them to buy local stocks.



SCMP Graphic

The influx has driven up the stock market. In eight days of trading the Hang Seng index has entered record-breaking territory.

The Government's financial gurus are worried because the Hong Kong dollar needs to stay close to a defined level of 7.80 to one US dollar. If the currency strays too far from that level, it will create uncertainty in financial markets and erode business confidence.

The Hong Kong Monetary Authority injected HK$1 billion early yesterday morning when the exchange rate reached HK$7.7230 to the US dollar – considered too far from the official level. At the end of the day it was 7.7250.

The peg with the US dollar was created after the territory's financial system collapsed 10 years ago.

The operation head for the authority, T. Y. Chan, said yesterday's move was aimed at stabilising the exchange rate.

He said the authority would closely monitor exchange rate movements, and if the situation warranted, other measures would be taken to defend the peg.

"We can either directly intervene in the market, that is, buying foreign currencies and selling Hong Kong dollars, or we can amend the bid and offer rate of the liquidity adjustment facility," he added.

The facility is a mechanism provided to banks through which overnight lending to and borrowing from the Exchange Fund is available. Changing the rates will alter the availability of funds to the banking sector.

Market practitioners generally felt that the strong Hong Kong dollar did not pose a serious threat to the exchange system, and the injection was more of a gesture than of any real use.

It is the third time this year that the Monetary Authority has mobilised its resources to help ease the liquidity in the market. But the previous two interventions, in which HK$650 million was injected each time, were spurred more by large-scale flotations.