



DAILY INFORMATION BULLETIN

Wednesday, December 13, 1972

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UNOFFICIALS SUPPORT ANTI-CRIME BILL

Community Behind Government In Combatting Crime

The Hon. P.C. Woo said today the community at large is solidly behind the Government in its determination to win the fight against violent crimes in Hong Kong.

He was speaking in the Legislative Council at the resumed debate on the second reading of the Public Order (Amendment) (No. 2) Bill 1972.

The bill proposes to introduce, among other things, a mandatory minimum sentence for possessing an offensive weapon in a public place without reasonable excuse, and to enable a police officer to search a person in a public place for any offensive weapon.

Mr. Woo said the bill has the full support of the Unofficial Members and "I think that everyone in his right senses should applaud Government's action."

After all, he said, the measures now proposed are to correct and restrain a situation which threatens to get out of control.

He said the existing penalty is no doubt suitable for normal times, but as far as violent crime is concerned, conditions at present are not normal in Hong Kong.

"In the circumstances which now face the Colony, I fully believe that the imposition of a mandatory minimum sentence for possession of an offensive weapon is justified," he said.

/Mr. Woo

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Mr. Woo also pointed out that Chinese thinking for centuries has been that "in normal times, reasonable penalties should be imposed; but in times of disorder, severe sentences must be passed to correct the situation."

He suggested that the peace of mind which every Hong Kong citizen expects can only be restored if steps are taken to prevent the undesirable element of the community from carrying offensive weapons.

He described the crime wave as "a challenge to our stability and to society itself" and said it is a cause for grave concern and there must be still more vigorous action.

Social Justice

Three other Unofficial Members, the Hon. Wilfred Wong, the Hon. T.K. Ann and the Hon. Wilson Wang, also spoke in support of the bill.

Mr. Wilfred Wong reiterated that "the role of an individual in society is not paramount but subservient to social justice" and said an individual is only useful if he is useful to society, but loses his value when he becomes a menace to society.

He described thugs as "a product of a permissive society" and said if there does not exist a sufficiently strong deterrent, they will keep on preying on their victims in Hong Kong.

He mentioned those who believed that a minimum sentence is inconsistent with modern concept of justice and pointed out "it is this very concept which led to the appalling crime rate in America,"

/Mr. Wong

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Mr. Wong also said if there are those who are thinking of a policeman planting an offensive weapon on an innocent individual, he would say this is unlikely because the policeman would be putting his future career in jeopardy.

Mr. Ann told the Council that "there is very seldom a bill that has received such wide support from the public like this one."

"The people feel relieved that violent crimes are beginning to be attacked on all three fronts: administratively, legislatively and judicially," he said.

Mr. Ann pointed out that fear of detection is only workable when there is fear of the penalty after detection, and said now that proposals are provided by the bill, "the initial successes will, I am sure, give to the people great encouragement to co-operate."

Minimum Sentences

In the long run, he said, minimum sentences proposed for robbery or serious assaults may be the "sine qua non for stamping out the spreading crimes."

However, he suggested that what is and is not an offensive weapon should be clearly expressed in Chinese language, that corrosive acid should be included, that more plainclothes policemen be employed "to watch the crime from within", and that the definition of "public place" be made more specifically known.

Mr. Wilson Wang, speaking in Cantonese, pointed to the "alarming" element of violence so often evident in robbery crimes and gang fights these days, and said the proposed mandatory minimum sentence is not unreasonable.

/"The proposal

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"The proposal can very well serve as a strong deterrent, as it seems that many thugs tend to ignore existing law," he said.

As to the proposed stop-and-- search power for a police officer, Mr. Wang drew the Council's attention to a suggestion that any search of such nature should be conducted by at least two police officers so as to provide a third-party witness.

Another point is that the search should be limited to uniformed police officers only and be conducted on production of credentials so as to avoid the question of imposters, he said.

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BRAVE ACT IN CRIME PREVENTION RECOGNISED

Two Members Of Public To Receive Ex-Gratia Awards

The Government is to award a total of \$17,500 to two members of the public in recognition of their brave act and public-spirited conduct in assisting the prevention of crime.

This was announced by the Acting Attorney General, Mr. G.R. Sneath, at the Legislative Council this afternoon when he moved two motions to grant ex-gratia awards to Mr. Cheung Kam-fai and the dependants of the late Mr. Ng Shung-por.

Under section 95 of the Interpretation Ordinance, Mr. Sneath said, the Council might award compensation to any person injured whilst carrying out a moral duty to assist in the prevention of crime.

Mr. Cheung, 20, was injured in August last year when he joined in a chase after an armed robber who later inflicted wounds on his chest and cheek with a knife.

As a result, Mr. Cheung had to remain in hospital for two days, and was off work for two weeks.

The award of \$500, Mr. Sneath said, was in recognition of his brave act and public-spirited conduct.

Referring to the case of the late Mr. Ng, Mr. Sneath, on behalf of the Council, expressed sympathy with the family in their sad loss.

/Mr. Ng,

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Mr. Ng, 22, died in a struggle with three armed robbers who intruded into his home in Yuen Long on January 26, this year.

"Mr. Ng himself had been contributing \$200 a month which was about one-third of the family income.

"The award of \$17,000 has been calculated as being a sum sufficient to replace the contributions which Mr. Ng could have been expected to make to the family had he lived; and in computing this figure the ages of his brothers and sisters were taken into account as one must assume that in due course they will earn and contribute to the family income," Mr. Sneath said.

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DECISION SOON ON ALLOCATING MARKET STALLS

In Hing Wah Estate

A decision is expected to be made early next year on how best to allocate the market stalls in the Hing Wah Estate, Phase I.

The Secretary for Housing, the Hon. I.M. Lightbody, said today it has recently be suggested that the problems presented by hawkers trading in the nearby Chai Wan Estate generally, should be looked at overall before a decision is made.

Speaking in reply to the Hon. Joyce Symons in the Legislative Council, he said a survey of hawkers in the area is proceeding and should be finished within this week.

After that, he said, there will be a joint study by Resettlement and Urban Services Department staff with a view to putting agreed proposals to the appropriate Select Committee of the Urban Council at its meeting in January next.

Mr. Lightbody said that although the modular market at Hing Wah Estate, Phase I, was completed about 18 months ago, the estate blocks had been fully occupied only in the last month or so, and as recently as August this year, the estate was only 80 per cent occupied.

"In this situation, it is better to have the residential blocks more or less fully occupied before leasing the market stalls," he said.

/In reply

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MORE OFFENSIVE TRADES AREAS TO BE SET ASIDE

Position On Sheung Shui Tanneries Outlined

The Government has already drawn up plans for a number of large sites to be set aside for more Offensive Trades areas, the District Commissioner, New Territories, the Hon. D.C. Bray, announced in the Legislative Council today (Wednesday).

No new offensive trades, he said, would be allowed to establish themselves outside these designated areas.

Referring to the tanneries at Sheung Shui, Mr. Bray said that twenty-one of them had already deposited sufficient land exchange entitlements to enable them to be allocated sites in the Offensive Trades Area in Kwai Chung.

These tanneries, he said, would be permitted to continue in business at Sheung Shui during the period required for the completion of land allocation formalities and the building of new factories.

But, while they are there, they will be required to comply with certain special conditions designed to minimise, as far as is practical, problems of pollution.

"They will furthermore have to meet a series of deadlines set to ensure steady progress towards completion of the new factories and failure to meet these will lead to their immediate clearance from Sheung Shui."

/Mr. Bray

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Mr. Bray said the remaining 34 tanneries, who were unable individually to acquire land exchange entitlements, had now found it possible to combine into two or three consortia with better prospects of being able to obtain the necessary finance.

He said they had until December 31 to do this and if they succeeded they would be treated in the same way as the first group. "If they fail, there will be no alternative but to clear them," he stressed.

Mr. Bray added that the Government had given the operators of the Sheung Shui tanneries every chance to re-establish themselves in conditions environmentally acceptable because they had been in operation for a long time -- some of them for more than twenty years.

"In any event," he said, "we feel that we have now gone as far as we can to accommodate the smaller operators who are bound to have difficulties in operating on an acceptable basis."

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CONTROL OF ADVERTISING SIGNS

Changes in Law Under Consideration

Urgent attention is being given to tighten existing regulations governing the installation and control of advertising and decoration signs.

This was stated today in the Legislative Council by the Director of Urban Services, the Hon. D.R.W. Alexander, in answer to a question raised by the Hon. Szeto Wai.

Mr. Alexander said that under the existing legislation the Director of Fire Services was authorised to order the removal or repair of any hoarding or structure which, in his opinion, constituted a fire hazard or obstructed fire escape exits in buildings.

Prior approval from the Director was also required for the erection of neon signs, and the Director was empowered to order the removal of such signs if they constituted a serious fire risk.

Mr. Alexander said the Director of Fire Services fully supported the proposed changes in the existing legislation.

"However, because of limitation of staff and the priorities set by the Fire Services Department, all affecting the well being and safety of the community, it will not be possible for the Director to embark on urgent action to order the removal of all signs contravening the regulations," Mr. Alexander said.

He added that the Director would continue to do whatever he considered necessary for this purpose.

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METHODS OF STREET CLEANSING TO BE MODERNISED

Recruitment Of Cleansing Workers Improved

The Urban Services Department is continually seeking ways and means of modernising and improving its present methods of street cleansing in order to move away from the existing labour intensive organisation.

The Director of Urban Services, the Hon. D.R.W. Alexander, stated this today in the Legislative Council in reply to the Hon. James Wu.

However, he said there are limitations to what that can be done and "we ourselves recognize the present shortcomings and need no prompting in our search for improvements which might be feasible in the Hong Kong situation."

The Director disclosed that since the introduction of the recent increase in wages and obnoxious duty allowance, there has been a marked improvement in the recruitment of labourers for the Cleansing Division of his department.

"Where earlier in the year, we had 300 vacancies, we now have only 50. However, the rate of turnover remains high," he said.

As regards the final disposal of refuse, Mr. Alexander said there is considerable difficulty in Hong Kong about finding suitable sites both for incinerators and dumps, but he assured the Council that the departments concerned have taken intensive action to solve this problem.

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HIGHER FINES FOR HARBOUR POLLUTION OFFENCES

An amending bill to provide increased penalties for permitting the discharge of oil either from ships or from the land may be introduced into the Legislative Council shortly.

The Acting Attorney General, the Hon. G.R. Sneath, said today that under the bill, the existing penalty of \$4,000 maximum would be replaced by a maximum fine of \$20,000.

Speaking in the Legislative Council in reply to the Hon. Wilson Wang, he said the most serious threat of pollution in Hong Kong's harbour and on beaches comes from oil which may be discharged from ships or even from shore installations.

"The problem has been recognised; and indeed a sub-committee of the Port Executive Committee has been set up to deal specifically with this matter," he said.

He said the amending bill has been submitted to the Executive Council, and authority has been given for its introduction into the Legislative Council pending any recommendations which the sub-committee may make.

He told the council that the threat of serious oil pollution from the sunken Queen Elizabeth ceased to exist on November 30 when the work of removing the oil from that vessel was completed.

So far as litter is concerned, Mr. Sneath said there is our new legislation with maximum fines which are given plenty of publicity.

There would seem to be no reason to suggest that these fines are inadequate seeing that they go up to \$2,000, he added.

CROSS-HARBOUR BRIDGE FEASIBILITY STUDY

Investigation Item Under Consideration

The Government is considering including an "Investigation" item in the Public Works Programme with a view to finding out whether the construction of a cross-harbour bridge is feasible within the restrictions imposed by marine and aviation requirements.

The Director of Public Works, the Hon. J.J. Robson, said this today in the Legislative Council in reply to the Hon. Szeto Wai.

Mr. Robson recalled that the Long Term Road Study Report published in 1968 clearly established that cross harbour movements would increase to such an extent that a second cross harbour crossing by road would be necessary in the future.

"I personally hold the view that Lei Yue Mun bridge is the obvious place to provide a second crossing of the harbour if this desire is to be met, though admittedly there are problems connected with the ships and aircraft which both pass through or over the gap," he said.

The Director said there have been preliminary discussions between himself and the Directors of Marine and Civil Aviation, and it seems possible that, in terms of the height to be adopted, an acceptable compromise might be reached for the construction of any future bridge.

"Nevertheless, before consideration can be given to the inclusion of a works item in the Public Works Programme for a project of this magnitude, it is necessary to assure ourselves that a bridge will not have adverse effect on other important considerations such as air safety and, in particular, the integrity of the Instrument Landing System for the Hong Kong Airport," he said.

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STATEMENT ON HONG KONG'S STERLING RESERVES

The Financial Secretary, the Hon. C.P. Haddon-Cave, today described the current year as an exceptional one in the international monetary field and said that many of the decisions taken in the financial capitals of the world have had a very special significance for Hong Kong.

Speaking in the Legislative Council this afternoon, he said that while our reserves had suffered serious losses in both Hong Kong and U.S. dollar terms it was a tribute "to the underlying strength of our position that confidence in the exchange stability of the Hong Kong dollar remains un-impaired."

The Financial Secretary said that at the time of the floating of the Pound Sterling, the value of the sterling assets held by the Hong Kong Government, including those bank-owned assets guaranteed under the Exchange Fund Guarantee Scheme, amounted to approximately £900 million.

In terms of Hong Kong dollars, the whole of the loss resulting from the complicated and quite unforeseen sequence of events following the decline in the value of Sterling from US \$2.6057 to US \$2.40 fell on public funds. The loss came to approximately HK \$890 million.

The Financial Secretary emphasized, however, that while this figure represented an "accurate picture" it should not be taken as "exact" since the rate not only continued to fluctuate but also the amounts held were constantly changing.

The losses, he said, should be viewed against the advantages Hong Kong had received from having invested in Sterling.

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"Interest rates in London have in general been higher than elsewhere," he pointed out. If these rates were taken at one per cent per annum higher then the extra interest would amount to some £30 million.

"This goes some way towards off-setting the capital loss we have now suffered. It is a fact that all countries with overseas reserves to invest find the choice of currency a difficult one," he said.

Those countries who chose the U.S. dollar, he noted, suffered a loss of 8.57 per cent last December and they had no guarantee at all against further losses.

While our Sterling Guarantee and its extensions to the banks through the Exchange Fund Guarantee Scheme had afforded us inadequate protection, "it has proved better than no guarantee at all," he said.

The Financial Secretary explained that the Government's surplus available for spending on future projects had been correspondingly reduced and he gave two reasons for this.

Firstly, the free surplus in the Exchange Fund -- that is the amount required to maintain the assets of the Fund at 105 per cent of the note issue -- would be largely used up in adjustment payments to the banks.

The second reason was that the Hong Kong dollar value of the sterling assets held on account of the General Account had been reduced.

Mr. Haddon-Cave estimated that the Colony's fiscal surplus at this time stood at about \$3,000 million as compared with \$3,900 at March 31, 1972.

These calculations, he said, did not take into account any fall in the market value of our securities nor the surplus accumulated so far this year.

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The Financial Secretary also told Council that Hong Kong's external reserves were still largely held in sterling securities.

It was possible, he added, to select a currency that would appear more likely to appreciate than depreciate in the short term. But one difficulty here was that "we tend to invest in the medium and long end of the market, in order to maximise earnings, and what may appear correct in the short term may prove very wrong in the longer term."

Mr. Haddon-Cave said decisions had to be taken with the longer term in mind because, in the uncertain foreign exchange markets of recent years, it had not been possible to move substantial sums from one currency to another quickly without unacceptable loss.

Another difficulty in the way of rapid diversification policy was that those currencies thought by the market in general to be under rather than over-valued were naturally in short demand.

"The result is that interest rates are extremely low or even negative," he said.

Mr. Haddon-Cave added: "Thus the attractions of switching out of sterling on a major scale, at least until September 1973 when the present agreement expires, are small."

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SEVEN BILLS PASSED IN LEGCO

Nine Sessional Papers Tabled

Seven bills passed their committee stage and third readings in Legislative Council this afternoon and became law.

They were the Law Amendment and Reform (Consolidation) (Amendment) Bill 1972; the Law Revision (Miscellaneous Amendments) Bill 1972; the Protection of Women and Juveniles (Amendment) Bill 1972; the Public Order (Amendment) (No. 2) Bill 1972; the Wild Birds and Wild Mammals Protection (Amendment) Bill 1972; the Supplementary Appropriation (1971/72) Bill 1972; and the Companies (Amendment) Bill 1972.

The Road Traffic (Amendment) (No. 2) Bill 1972 and the Workmen's Compensation (Amendment) Bill 1972 had their first and second readings. Debate on them was adjourned.

Debate on the second readings of the Law Amendment and Reform (Consolidation) (Amendment) Bill 1972; the Law Revision (Miscellaneous Amendments) Bill 1972; the Protection of Women and Juveniles (Amendment) Bill 1972; the Public Order (Amendment) (No. 2) Bill 1972; the Wild Birds and Wild Mammals Protection (Amendment) Bill 1972; and the Supplementary Appropriation (1971/72) Bill 1972 was resumed.

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Nine sessional papers were tabled in the Council this afternoon. They were the Annual Report of the Hong Kong Productivity Council for the year 1971-72; the Annual Report by the General Manager, Railway for the year 1971-72; the Report by the Commissioner for Transport for the year 1970-72; the Annual Report of the London Office for the year 1971-72; the Report of the Brewin Trust Fund Committee on the Administration of the Fund for the year ending June 30 1972; the Annual Report by the Director of Social Welfare for the year 1971-72; the Annual Report by the Director of Immigration for the year 1971-72; the Annual Report by the Commissioner of Inland Revenue for the year 1971-72; and the Annual Report by the Commissioner of Prisons for the year 1971-72.

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BY-PRODUCT PLANT TO BE IMPROVED

\$2.5 Million Project For Kennedy Town Abattoir

The by-product plant at the Kennedy Town Abattoir is to be modernised and expanded to achieve maximum efficiency and productivity.

A "close-circuit" system consisting of automatic handling, milling and packing equipment, and a number of additional cookers and boilers are to be installed.

When these new installations are completed, the number of workers in the plant can be reduced, with quality control imposed, and possible contamination problems eliminated.

The main by-products manufactured by the plant are meat-and-bone meal, blood meal and industrial grease.

The total revenue collected from the sale of these by-products amounts to more than \$1 million each year; and with the modernisation and expansion of the plant, the amount is expected to double.

Sources of material for the by-products are the two abattoirs at Kennedy Town and Cheung Sha Wan, where 7,000 pigs and 500 heads of cattle are slaughtered daily.

The estimated cost of the project is \$2.5 million.

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HIGH HONOURS FOR H.K. POLYTECHNIC LECTURER

A lecturer of the Hong Kong Polytechnic has recently been awarded the Silver Medal of the Society of Dyers and Colourists commonly known as A.S.D.C.

Several former students of the Institute have been awarded high honours by the Society.

The lecturer is Mr. Chan Ka-ku, who is in charge of the Higher Diploma Course in Dyeing, Printing and Finishing Technology in the Department of Textile Industries at the Polytechnic.

The A.S.D.C. Silver Medal was awarded to him in recognition of his services to education in colour technology in Hong Kong.

Mr. Chan joined the Department of Textile Industries eleven years ago. He has been directly involved in the development of the Higher Diploma Course in Dyeing, Printing and Finishing Technology to the present well-established academic standard.

Two former students of the Higher Diploma Course, who have successfully completed this year's A.S.D.C. examination and fulfilled its regulations, have been elected Associates of the Society.

They are Mr. Chan Kah-key and Mr. Yeung Kwok-wing.

A third former student, Mr. Chaing Ka-ping, has been awarded the highest honour of the A.S.D.C. examination -- the President's Diploma of Honour.

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Nineteen other former students of the Course have also successfully completed the same examination.

Apart from a few who are at present pursuing further study in universities overseas, the rest of the students are now employed in the local textile dyeing and finishing industry.

They will no doubt play an important role in the improvement of techniques and production methods in the local dyeing industry in future.

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LEGCO PROCEEDINGS RECORDED

Note to Editors: The proceedings in today's Legislative Council meeting have been recorded. You are welcome to consult the tapes at the Press Room, Government Information Services.

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WATER INTERRUPTION

Water supply to a number of premises in Yau Ma Tei, Kowloon, will be interrupted for five hours from 1 a.m. to 6 a.m. tomorrow (Thursday).

The temporary stoppage is to enable the Waterworks Office to carry out a leakage test.

The area to be affected is bounded by Saigon Street, Nathan Road, Jordan Road and Shanghai Street.

A number of premises in Mong Kok will also have their water supply interrupted for five hours from 1 a.m. to 6 a.m. on Saturday, December 16.

The Waterworks Office will carry out a leakage test during the period of stoppage.

The area to be affected is bounded by Nelson Street, Argyle Street, Nathan Road, Mong Kok Road and Sham Chun Street.

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Release time: 9.30 p.m.



DAILY INFORMATION BULLETIN

SUPPLEMENT

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SPEECH BY THE HONOURABLE THE FINANCIAL SECRETARY
IN LEGISLATIVE COUNCIL ON WEDNESDAY, 13TH DECEMBER 1972

Mr. P.C. Woo:

Is the Financial Secretary yet in a position to make a statement on his recent discussions in London on the Sterling Guarantee Agreement and the security of Hong Kong's sterling reserves?

Reply:

Yes Sir,

Introduction

But, if I am to put my talks in London in November in perspective, I am afraid I shall have to speak at some length. I do not apologize for this. Our financial and monetary stability is fundamental to our well-being and I can well understand that honourable Members and the public at large wish to be assured that this Government has acted at all times to secure Hong Kong's best interests. This is always our purpose though our actual performance is sometimes under the control of prevailing circumstances and external events over which no individual government can exercise very much influence.

Historical Background

May I begin, Sir, by reminding honourable Members of the historical background to the Hong Kong dollar's link with sterling? Until 1935 Hong Kong

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had a variable exchange relationship with London because the sterling (or gold) value of the Hong Kong dollar varied with the price of silver. But this had the advantage of establishing a stable exchange relationship with China whose currency was also based on a silver standard and thus of preserving the stability of the entrepot trade on which Hong Kong's economy then largely depended. When China abandoned the silver standard in 1935, Hong Kong followed. The note issuing banks were obliged to surrender all silver previously held by them against their note issues in exchange for certificates of indebtedness. The silver surrendered by the banks was used to set up an Exchange Fund which, from the outset, kept its assets in sterling, a not surprising move given the range of banking and investment facilities available in London. The Fund buys and sells sterling at fixed rates close to par - or did so until sterling floated - and thereby regulated the exchange value of the Hong Kong dollar. The sterling area as it is known to-day came into being in the early days of the last war basically as an aid to assuring that the foreign earnings of the Commonwealth were centralised for the common good. Hong Kong, then, became a member of the sterling area which in effect meant that the Government's reserves and the greater part of the reserves of the banking system had to be kept in London in sterling assets.

In 1935 the exchange value of the Hong Kong dollar was fixed at approximately 1/3d. or at a rate of HK\$16 to the £ sterling; and, with the setting up of the International Monetary Fund after the war, the Hong Kong dollar was given a gold parity which reflected this rate. Together with most other sterling area currencies - and indeed those of a large number of other countries as well - Hong Kong followed Britain when sterling was devalued in terms of the U.S. dollar in 1949. This strengthened the view widely held in

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commercial and banking circles that the relationship between the Hong Kong dollar and sterling was fixed. So much so that, for instance, it was not the custom for importers or exporters with sterling contracts to cover forward; and the authorized banks, required as they were by the exchange control rules of the sterling area to hold their excess liquidity in sterling, did not envisage an exchange risk.

So, although the relationship between the Hong Kong dollar and sterling was at no time a statutory one, but one that was established and maintained by the operations of the Exchange Fund, it came to be regarded as immutable. The Hong Kong dollar, if you like, was looked upon almost as an extension of sterling, despite the fact that the money supply was based on Hong Kong's own net foreign exchange earnings (largely in U.S. Dollars and an inflow of capital largely from South East Asia.)

In November 1967 when sterling was devalued by 14.3% Hong Kong was faced with the dilemma of either again following sterling down and letting the internal cost/price structure adjust to the new rate through inflation or of maintaining the cross rate with the U.S. dollar and taking a loss on the Hong Kong dollar value of both the Government's and the banking system's sterling reserves. In the event, a compromise solution was adopted: the Hong Kong dollar was devalued by 5.7% in terms of the U.S. dollar, that is to say, the old rate of H.K. \$16 to the £ sterling was changed to HK \$14.54. This compromise solution cost Hong Kong public funds about H.K. \$450 mn., including ex gratia adjustment payments from the Exchange Fund to the commercial banks to compensate them for their losses. But it did allow us to limit the rise in our cost/price structure and it must be remembered that, in 1967 in contrast to 1949, very few countries even in the sterling area

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followed sterling down. After these events Hong Kong's recorded sterling assets amounted to £350 mn.

Both the Hong Kong Government and the authorized banks found themselves in a difficult position: on the one hand, the sterling area exchange control rules applied, thus effectively limiting our ability to diversify our external assets; on the other hand, if there were to be a further devaluation of sterling it seemed unlikely that Hong Kong would wish to follow suit, for our rate of exchange must be determined solely by reference to Hong Kong's own essential interests. In any case, even if we were ever to get into serious balance of payments difficulties, an adjustment in the rate of exchange would not, I am afraid, be a very appropriate way to deal with the situation because of our extreme dependence on foreign trade. Hong Kong's imports are equal to about 100% of the G.D.P. and exports to about 85%. Thus internal expenditure is reflected directly in expenditure of foreign exchange; and the best - and indeed the automatic - corrective to any disequilibrium (either way) in our balance of payments is an automatic monetary deflation (or inflation) which adjusts the cost/price structure until equilibrium is restored at the existing exchange rate. There is a continuous process of adjustment of this nature. When the balance of payments is in deficit, the full deflationary effect of this automatic mechanism is, in practice, softened by the availability of the Government and the banks of substantial external reserves; and, when the balance of payments is in surplus the inflationary effect of the automatic mechanism is to some extent limited by the issue of Hong Kong dollar currency only against the deposit of sterling and the requirement that the banks must

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maintain a liquidity ratio (cash/deposits) of 25%. As there are very few forms of liquid assets available internally (there is, for example, no short term Government debt as a vehicle for liquidity) this means that the banks have to maintain substantial external reserves.

After the devaluation of sterling in November 1967, the British Government was faced with a possible break-up of the sterling area and yet was unable to finance a substantial movement out of sterling into other foreign currencies such as U.S. dollars, because of Britain's own depleted reserves, and the fact that the devaluation took a long time to bring the balance of payments into surplus. So a line of credit of U.S. \$2000 mm. was negotiated with the Group of Ten (the so called Basle Agreement) which in turn enabled a free guarantee, to be offered by the British Government, of the U.S. dollar value of their official sterling reserves to all members of the sterling area, including Hong Kong. This guarantee was in respect of all officially held sterling in excess of 10% of each country's total official external reserves. The guarantee was offered subject to each country maintaining a minimum proportion of its reserves in sterling, roughly the proportion in sterling when the offer was made. For some countries the guarantee was for three years and for others (including Hong Kong) it was for five years from 25th September 1968.

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The Two Guarantee Agreements (S.G.A. & E.F.G.S.)

Our Sterling Guarantee Agreement with the British Government includes provision whereby part of the banking system's sterling reserves are counted as official reserves for the purposes of the guarantee. The banking system's sterling assets differ in important respects from the Government's, both as to the purpose for which they are held and the form in which they are invested. They are held by a large number of banks, some large and some small, they fluctuate widely, and they must at all times be available to meet the banks' obligations, a large part of which are in the form of Hong Kong dollar liabilities. It was not easy to devise a system of bringing these funds within the protection of the Sterling Guarantee Agreement while retaining their essential purpose and character. The solution adopted was the Exchange Fund Guarantee Scheme whereby the Exchange Fund entered into a series of guarantee agreements with the banks which wished to participate. (To limit the cost of this scheme to the Exchange Fund those banks which did choose to join were required at all times to keep a substantial proportion of their external funds within the scheme). The operation of the scheme, coupled with Exchange Control restrictions on the Authorized Banks, meant that a very high proportion of the banks' external assets, which were steadily increasing anyway, came to be covered over the last four years.

I should like to emphasize here the main differences between the Sterling Guarantee Agreement with the British Government and the Exchange Fund Guarantee Scheme with the banks. Under the Sterling Guarantee Agreement the British Government guarantees without charge the U.S. dollar value of 90% of the

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eligible sterling asset held by the Hong Kong Government including 90% of the eligible sterling asset owned by the banks and brought into official hands through the Exchange Fund Guarantee Scheme. Under this scheme - the Exchange Fund Guarantee Scheme - the Exchange Fund guarantees to the banks the Hong Kong dollar value of 100% of the sterling covered under the scheme and a small charge is made.

The Sterling Guarantee Agreement is first implemented if the sterling/U.S. dollar rate falls below US \$2.40 by more than 1% for a continuance period of 30 days. Then the British Government is obligated to pay to the Hong Kong Government, for account of the Exchange Fund, sufficient sterling to restore the U.S. dollar value of the guaranteed proportion of our official sterling reserves. Thus, providing there was no significant fall in the total of bank owned sterling assets between the date the sterling rate was floated and the date the rate first fell below US \$2.40 by 1%, the burden of adjustment payments from the Exchange Fund to the banks in respect of any fall in the rate below U.S. \$2.40 will be largely met - to the extent of 90% - by compensation payments to the Exchange Fund by the Bank of England on behalf of the British Government. If the sterling/US dollar rate falls further and subsequent implementations are necessary the position is the same, provided again there has been no significant fall in bank owned sterling. The Exchange Fund Guarantee Scheme is implemented in respect of any fall in the fixed rate between the Hong Kong dollar and sterling. Adjustment payments have to be made to the participating banks so as to restore the Hong Kong dollar value of the sterling covered, but,

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unlike the Sterling Guarantee Agreement which provides for continuous settlements, payments under the Exchange Fund Guarantee Scheme will be made in one amount when sterling ceases to float.

Growth of Sterling Balances

So, following the negotiation of the Sterling Guarantee Agreement, we remained locked into sterling. But, unlike the 32-year period from 1935 to 1967, an exchange risk was now explicitly recognized and covered. As it happens, the conclusion of this Sterling Guarantee Agreement coincided with the beginnings of a period of rapid and sustained growth of our economy. As a result the sterling assets of the banking system increased from about £200 mn. at the end of March 1969 to about £360 mn. by the end of March 1972. At the same time substantial budgetary surpluses amounting in all to HK\$1,915 mn. in the four years 1968-69 to 1971-72 were realised and this money was largely invested in sterling securities the rest being deposited locally with our bankers. As a result of this and other factors the Government's own sterling assets increased from £190 mn. at the end of March 1969 to £408 mn. at the end of March 1972.

Extension of Sterling Guarantee Agreements

Meanwhile, in the late summer and autumn of 1971 the U.S. dollar came under pressure in the world's foreign exchange markets. It was for this reason that we did not immediately take advantage of the lowering of the minimum proportion of our total official external reserves which we undertook to keep in sterling under the Sterling Guarantee Agreement. A general lowering of the M.S.Ps. by 10% (meaning in our case from 99% to 89%) was offered by the

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British Government as part and parcel of a renegotiation for a further two years from 25th September 1971 of the terms of the three year Sterling Guarantee Agreements and naturally this concession was extended to those countries with five year agreements.

1971 International Monetary Crisis

The U.S. dollar crisis was resolved by the Smithsonian settlement announced on 19th December. For a variety of reasons, which I explained at length in an adjournment debate in this Council on 5th January last, the Government decided to maintain the gold parity of the Hong Kong dollar, thereby revaluing against the U.S. dollar by 8.57% and maintaining the then Hong Kong dollar/sterling parity. So this decision had no implications for the value in Hong Kong dollar terms of our external exchange reserves given that they are - or were then - almost entirely held in sterling. However, the British Government insisted that the sterling balances of all countries with whom they had entered into agreements remained guaranteed at US \$2.40, that is to say, that the new Sterling/U.S. dollar rate of US \$2.6057 was not applicable. Yet we immediately realised that any devaluation of sterling which was not followed by an adjustment of the Sterling/Hong Kong dollar rate would mean that the Hong Kong dollar value of the banks' sterling assets would have to be restored through the Exchange Fund. This was the origin of many subsequent difficulties.

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During the first half of 1972 our sterling reserves continued to rise: the export trend was weaker than in earlier years but so was the import trend and other factors - tourism, invisibles and the capital account - exhibited continuing strength. By the end of May they stood at £803 mn. of which £418 mn. was on Government account and £385 mn. belonged to the banking system and was covered by the Exchange Fund Guarantee Scheme.

As soon as the 1972-73 budget was out of the way I went to London to clarify certain aspects of the 10% diversification facility accorded us in the previous September. With the agreement of the banks, I subsequently decided that the facility should be utilized solely in respect of Government owned sterling assets as the banks enjoy a 100% guarantee against a fall in the exchange value of sterling in terms of Hong Kong dollars; and there would have been technical difficulties in sharing this facility with the banks. I pressed, but unsuccessfully - and so did several other Governments - for a revision of the rate at which the guarantee would be implemented and, failing this, for an early re-negotiation of the Agreement, the revised agreement to be for a further period beyond September 1973 and effective before the present Agreement expired. And, as I told honourable Members in this Council on 10th May last, I argued that the revised Agreement should "reflect present day and not 1968 realities". I meant by this that the guarantee rate should be the rate of the day and that our M.S.P. should be further reduced.

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Floating of Sterling

Then came the sudden and unexpected decision of the British Government on 23rd June to allow sterling to float for the time being. While there had been some speculation that cost-push inflation, efforts to expand the British economy and the impact of entry into the European Economic Community would sooner or later require a downward revision of the Smithsonian rate of US\$2,6057, the reason for this decision was the large movement of funds out of sterling during the previous few days which the British Government did not consider justified by the objective facts of the country's balance of payments position.

Dismantling of the Sterling Area

At the same time, the British Government announced the extension of exchange control to Overseas Sterling Area countries to prevent disruptive outflows of U.K. resident funds. Hong Kong became part of the External Account Area. In effect, the sterling area was dismantled and the barrier around sterling withdrawn from the sterling area as a whole to the British Isles.

The previous position was that sterling funds held by residents of OSA countries could not be transferred into foreign currencies except for genuine trading purposes. Since 24th June residents of OSA countries have been free to transfer their sterling funds into any currency for any purpose. Of course, in Hong Kong foreign currencies have always been purchasable in the free market operated by the non-authorized banks.

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But the immediate question which arose, now that the banks previously authorized to deal in foreign currencies (the so called Authorised Banks) did not have to hold their excess liquidity in sterling, was whether the Exchange Fund should continue to offer cover for further accruals of excess liquidity in sterling. The banks now had the choice, exchange control having ended, of placing their excess liquidity in sterling or non-sterling assets. Why therefore should the Exchange Fund offer cover, at any rate during the period of the floating of sterling, thereby adding to the risks assumed?

Hong Kong's Reaction to Float

But a more immediate question to be answered was which of three options open to us should we follow during the floating of sterling, namely,

- (1) to remain linked to sterling at the then present rate of HK\$ 14.54 or at some other rate of our choice and thereby float with sterling;
- (2) to abandon the sterling link and replace it with a direct link with the US dollar;
- (3) temporarily to float the Hong Kong dollar independently with a view to establishing the true market valuation of the Hong Kong dollar in relation to other currencies.

As is now a matter of history we decided that the best course to adopt in the long run would be the setting of a new fixed rate between sterling and the Hong Kong dollar, for the fact is that Hong Kong's monetary system

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is closely linked to sterling and the greater part of our reserves are, as a matter of fact, in sterling. However, to have adopted this course straight away would have had the disadvantage that the Hong Kong dollar would still be floating with sterling albeit at a different rate; and so we decided, as an interim measure, to establish a direct link with the U.S. dollar at a little below the cross rate established in December last year. Thus we insulated the Hong Kong dollar from the effects of the floating of sterling.

Before the floating of sterling the cross rate between the Hong Kong dollar and the U.S. dollar only moved in response to the movements of the sterling/US dollar rate within the band of $4\frac{1}{2}\%$. But with the Hong Kong dollar linked directly to the U.S. dollar the rate could move in response to market forces affecting the Hong Kong dollar as such. As with any economy, there are always differences of timing between purchases of foreign currencies by our importers and other traders and the sales of such currencies by our exporters which causes the rate to move for short periods in either direction. But under the rules of the International Monetary Fund the rate has to be contained within a $4\frac{1}{2}\%$ band and so the Hong Kong Government is now obliged, whenever necessary, to maintain the rate within the band by selling U.S. dollars for Hong Kong dollars when the rate approaches the lower limit of HK\$5.7771 and selling Hong Kong dollars for U.S. dollars when it approaches the upper limit of HK\$5.5229.

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Consequences of Temporary Link with U.S. Dollar

A decision to delay the re-establishment of a new fixed rate between the Hong Kong dollar and sterling meant that the Exchange Fund Guarantee Scheme with the Hong Kong banks could not be implemented and, as the floating of sterling continues, we still do not know the extent of the liability of the Exchange Fund to restore the Hong Kong dollar value of the banks' holdings of sterling assets. But, so far, with the Sterling/US dollar rate at around US \$2.35 the cost is £46 mn. (or HK \$609 mn.) less about £9 mn. in respect of payments due under the Sterling Guarantee Agreement for the loss on 90% of eligible assets between US \$2.40 and 2.35 and less about £1 mn., being charges levied on the banks for cover. In other words, the net loss amounts £36 mn. Similarly, we do not yet know the exact extent of the loss in the Hong Kong dollar value of the sterling assets used to cover the note issue and the loss in the Hong Kong dollar value of the sterling assets belonging to the General Account, the Coinage Security Account and the Rehabilitation Loan Sinking Fund but, at US \$2.35, the loss is about £38 mn. After allowing for compensation payments for the loss on 90% of the assets between US \$2.40 and 2.35, which amounts to £7 mn., the net loss is about £31 mn.

Meanwhile, we were concerned about the future: in the short term up to the re-fix of sterling and in the longer term. By 6th July, the day on which we announced the linking of the Hong Kong dollar with the U.S. dollar, total sterling balances amounted to about £900 mn., an increase of £97 mn.

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since the end of May and largely due to an increased demand for cover from the banks. Pending clarification of the British Government's intentions for the future we told the banks that, whereas their 6th July sterling positions would remain covered, further accruals would not be accepted for cover. By this decision we at least limited the amount of bank sterling covered, since honourable Members will appreciate that on all bank sterling guaranteed the Exchange Fund remained at risk between US\$2.6057 and US\$2.40. Moreover, the extension of the scheme to accruals would, in the absence of a fixed Sterling/Hong Kong dollar rate, present considerable technical difficulties. The British Government accepted that, in the new situation, we had no obligation to add further bank funds to our total official external reserves and with it an obligation to maintain a proportion (89%) of such further additions in sterling.

July Talks and Later Contacts with London

Honourable Members will recall that soon after the British Government decided to float sterling, six teams of officials were sent out to sterling area countries to discuss the future of the Sterling Guarantee Agreements in the light of the new circumstances then prevailing. We held discussions with the team which visited Hong Kong between 14th and 17th July. I was at pains to point out to the team that, as sterling floated down from US\$2.6057, the value of our external reserves (which are largely in sterling) fell in relation to other currencies and in terms of the Hong Kong dollar; and I put to the British officials our views as to how our position should be protected, both during the remaining period of the float and after sterling had re-fixed with

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the U.S. dollar. We had in mind a new agreement to replace the present agreement and to run through perhaps to 1975, At that time we expected the discussions to be resumed at an early date. but some other sterling area countries were not willing to commit themselves to a renegotiation of the Agreements and the British Government, for its part, was not willing to negotiate with some countries only. We regarded this situation as entirely unsatisfactory from our point of view and kept up a telegraphic correspondence with London stressing the need for an early resumption of the July talks. As part of this process I called on Treasury officials in London in September. I said that, provided the terms were right we were willing to enter into another agreement for a period of, say, three years; and that, while we understood that there might be good reasons why other countries did not wish to commit themselves at that stage, their positions were different to Hong Kong's and their needs likewise. For instance, the minimum proportions of their external reserves (their M.S. Ps.) which have to be kept in sterling are much lower than Hong Kong's 89%.

So we kept on representing to the British Government that, if the Sterling Guarantee Agreements could not be re-negotiated before the spring of next year so that all concerned would know where they stood then at least the British Government should recognize that we were placed - and through no fault of our own - in a peculiarly difficult position. Both the Hong Kong Government and the banks faced the possibility of having a large unprotected sterling position at the expiry of the present Agreement

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on September 24, 1973, for it was impossible to forecast whether a new agreement on acceptable terms could be negotiated; and if it could not, there would be little time to re-deploy some of our locked in sterling assets so as to spread our exchange risks. We regarded, and still regard, a satisfactory new agreement as the best solution (even though it might mean taking powers to control the banks foreign currency holdings) since we could then continue to enjoy the advantages of investing in the London gilt edged market without risk. In this situation it seemed wiser not to wait for the re-negotiation but to make an alternative arrangement.

November Talks in London

Eventually, further talks were arranged in London last month and the outcome was an arrangement whereby, just as we are now under no obligation to take further accruals of bank funds into official hands and cover the amounts concerned through the Exchange Fund Guarantee Scheme, which is between the Hong Kong Government and the banks, so it was accepted that, if they wished, the banks holding the largest amounts could start to take some of their sterling assets out of the Scheme, subject to certain perfectly reasonable safeguards. This arrangement means that the figures of both total official external reserves and total sterling reserves used for the purposes of the Sterling Guarantee Agreement will fall by equal amounts and does not affect, in any way, the Hong Kong Government's obligation under the Sterling Guarantee Agreement to maintain the M.S.P. at 89%. But it does mean that the automatic channelling of bank funds into sterling assets which

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the 1968 Agreements brought about and which was halted by our action in July this year can now be partially reversed. In other words, a small part of the banks' sterling reserves which has been classified as official sterling reserves for the purposes of the Sterling Guarantee Agreement will revert to its former private status and will no longer be guaranteed.

Implementation of S.G.A.

After an initial plunge which de-fused the speculative pressures which gave rise to the decision to float sterling in the first place, the U.S. dollar/sterling rate hovered around \$2.45 for some 10 weeks and then at the end of September the rate began to fall again until it went below the trigger point of \$2.3760 on 24th October and remained there for a continuous period of 30 days. Accordingly, on 23rd November the British Government announced that the guarantee would be implemented and called for the necessary returns of total official external reserves and the actual sterling assets held on the appropriate dates. The closing rate on the 23rd November was US\$2.3506 and the first adjustment payments from the British Government will be based on this rate. If the rate should fall below this level by more than 1% for further periods of 30 days further adjustment payments will be due. Contrariwise, if there is any recovery before the establishment of a new fixed rate with the U.S. dollar, refunds will have to be made. But even after the re-fix the Sterling Guarantee Agreement will remain in force until 24th September 1973.

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So within the limits of the present Agreement (the operative rate of US\$2.40 and 90% cover) the floating of sterling has in no way affected our rights (or our obligations in respect of the M.S.P.). But, of course, the revaluation of sterling in December 1971 followed by the float downwards has cost us dearly between US\$2.6057 and US\$2.40 and so, as I say, we have all along pressed the British Government for early clarification of their intentions after September 1973. In addition, I shall be making it clear to the banks that any resumption of cover under the Exchange Fund Guarantee Scheme after the re-fix would be on revised terms, that is to say, the charges levied would have to reflect the risk taken by the Exchange Fund, taking into account all the circumstances at the time.

Assessment

Sir, the value of the sterling assets held by the Hong Kong Government, including those bank owned assets guaranteed under the Exchange Fund Guarantee Scheme, at the time of the float was approximately £900 mn. In Hong Kong dollar terms the whole of the loss resulting from this complicated and quite unforeseen sequence of events following the decline in the value of sterling from US\$2.6057 to US\$2.40 and amounting to approximately HK\$890 mn. falls on public funds. This figure cannot be exact because not only is the rate fluctuating, but the amounts held are changing daily. Nevertheless, the figures I have given presents an accurate enough picture. It means, of course, that the Government's surplus available for spending on future projects is correspondingly reduced for two reasons: in the first place, the free surplus

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in the Exchange Fund (i.e. the amount required to maintain the assets of the fund at 105% of the note issue) will be largely used up in adjustment payments to the banks (but let me hasten to add that the purpose of the Exchange Fund is to regulate the exchange value of our currency); and secondly the Hong Kong dollar value of the sterling assets held on account of the General Account has been reduced. I estimate that the Colony's fiscal surplus is at this time about \$3,000 mn. compared with \$3,900 mn. at 31st March. I am ignoring for the purposes of this calculation any fall in the market value of our securities, on the one hand, and the surplus accumulated so far in this year's accounts.

But these losses must be viewed against the advantages we have received from having invested in sterling. Interest rates in London have in general been higher than elsewhere. If one were to take those rates as 1% p.a. higher and I would have thought that the differences may have been greater than this over the five year period since the last sterling devaluation the extra interest would amount to around £30 million. This goes some way towards offsetting the capital loss we have now suffered. It is a fact that all countries with overseas reserves to invest find the choice of currency a difficult one. Those who chose the US\$, for example, suffered a loss of 8.57% in December 1971 and such holders have no guarantee against further loss. Our Sterling Guarantee Agreement and its extension to the banks through the Exchange Fund Guarantee Scheme has, in the event, afforded us inadequate protection, but it has proved better than no protection at all.

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Hong Kong's external reserves are still largely held in sterling securities. But as a result of the recent agreement the historical and technical factors which have led the banks to continue to increase their sterling assets have been in part reversed. It is, of course, possible to select a currency that seems more likely to appreciate rather than depreciate, in the short term. One difficulty here is that we tend to invest in the medium and long end of the market in order to maximise earnings and what may appear correct in the short term may well prove very wrong in the longer term. In the uncertain foreign exchange markets of recent years it has just not been possible to move substantial sums from one currency to another quickly without unacceptable loss, so that decisions have to be taken with the longer term in mind. A further difficulty in the way of a rapid diversification policy is that those currencies thought by the market in general to be under rather than over valued are naturally in short term demand. The result is that interest rates are extremely low or even negative and the Governments concerned impose restrictions to deter overseas investment in their currencies. Thus the attractions of switching out of sterling on a major scale, at least until September 1973 when the present Agreement expires, are in fact small.

Nevertheless as suitable opportunities occur we are and have been reducing the proportion of our reserves held in sterling to take advantage of our 10% diversification facility. This has necessarily been a slow process because nothing would have been gained by switching out of sterling into

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other currencies in anticipation of a depreciation in the value of sterling to its guarantee level of US\$2.40 to £1 unless the benefits from such movements were likely to be sufficient to at least offset losses in earnings resulting from the interest rates in other financial centres being generally much lower than in London. Some sales of gilt edged securities have been made to provide funds for buying foreign currencies but, because the London gilt edged market has been weak it would not, for obvious reasons, have been prudent to make large scale sales of gilt edged securities. As sterling fixed deposits and other investments mature we have switched these into foreign currencies and our sterling interest earnings, which are in excess of £30 million (about 12% of recurrent revenue) a year, have been similarly re-employed outside London. While the sterling/dollar exchange rate is below US\$2.40 to £1 we run the risk of incurring a further loss in the value of our overseas reserves if we switch out of sterling. This is because sterling switched into other currencies while the guarantee is operative would cease to be eligible if the average rate of exchange does not fall by 1% or more between settlement dates. For these reasons we have had to slow down our diversification programme since 25th October, the date sterling fell for the first time below US\$2.40 to £1.

Conclusion

Sir, it is almost exactly a year since the Smithsonian settlement announced on 19th December 1971. It has been an exceptional year in the international monetary field and for Hong Kong many of the decisions taken in the financial capitals of the world have had a very special significance.

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Yet, while our reserves have suffered serious losses in U.S. dollar and Hong Kong dollar terms it is a tribute to the underlying strength of our position that confidence in the exchange stability of the Hong Kong dollar remains unimpaired, and I hope honourable Members will bear this in mind when making their own assessment of the Hong Kong Government's management of our monetary affairs over the past few years.

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Release time: 9.30 p.m.