

**Exchange Fund
Currency Board Account
as at 31 December 2010
(Expressed in millions of Hong Kong dollars)**

	Notes	31 December 2010 (Market Value)	30 November 2010 (Market Value)
MONETARY BASE			
Certificates of Indebtedness		226,705	218,125
Government-issued currency notes and coins in circulation		8,929	8,862
Balance of the banking system		148,702	148,740
Exchange Fund Bills and Notes issued	3,4	655,220	689,727
Interest payable on Exchange Fund Notes		327	695
Net accounts (receivable)/payable	3,5,7	(355)	(35,379)
Total	1,3	1,039,528	1,030,770 (a)
BACKING ASSETS			
Investment in designated US dollar assets		1,119,691	1,155,373
Interest receivable on designated US dollar assets		1,404	1,210
Net accounts receivable/(payable)	6	-	(42,178)
Total	2	1,121,095	1,114,405 (b)
BACKING RATIO [(b) / (a)] * 100%	8	107.85%	108.11%

Notes :

1. Movements in the Monetary Base during the period were as follows:

	<u>HK\$ million</u>
Balance brought forward	1,030,770
Increase/(decrease) in Certificates of Indebtedness	8,580
Increase/(decrease) in Government-issued currency notes and coins in circulation	67
Net issue/(net redemption) of Exchange Fund Bills and Notes	(34,155)
(Increase)/decrease in Exchange Fund Bills and Notes issued but not yet settled	34,664
Accrued interest on Exchange Fund Notes	177
Settlement of accrued interest on Exchange Fund Notes	(545)
Amortised discount/(premium) on Exchange Fund Bills and Notes	130
Revaluation losses/(gains) relating to Exchange Fund Bills and Notes	(482)
Settlement of accrued interest income/(expenses) on interest rate swaps	74
Net interest expense/(income) on interest rate swaps	(36)
Revaluation losses/(gains) relating to interest rate swaps	322
Increase/(decrease) in balance of the banking system (other than due to Discount Window Operations)	(38)
Balance carried forward	<u>1,039,528</u>

2. Movements in the Backing Assets during the period were as follows:

	<u>HK\$ million</u>
Balance brought forward	1,114,405
Increase/(decrease) on issue/(redemption) of Certificates of Indebtedness	8,580
Increase/(decrease) on issue/(redemption) of Government-issued currency notes and coins in circulation	67
Interest from investments	642
Revaluation gains/(losses) relating to investments	(2,599)
Balance carried forward	<u>1,121,095</u>

3. Discount Window Operations:

- (i) Discount Window Operations involve Hong Kong dollar overnight advances made to banks by way of crediting their accounts maintained with the HKMA (which is part of the balance of the banking system) on discounting Exchange Fund Bills and Notes. In accordance with generally accepted accounting practice, the Exchange Fund Bills and Notes discounted with the HKMA are not accounted for as reductions in the liabilities of the HKMA but are regarded as securities held against the advances so made.
- (ii) For the purpose of this Account, the advances to banks secured on Exchange Fund Bills and Notes are shown as deductions in arriving at the Monetary Base. There were no such advances at 31 December and 30 November 2010.

4. Interest payments on Exchange Fund Bills and Notes:

- (i) Starting from 1 April 1999, interest payments on Exchange Fund Bills and Notes have been allowed to increase the amount of outstanding Exchange Fund paper.
- (ii) During December 2010, the nominal value of Exchange Fund Bills and Notes decreased from HK\$687.10 billion to HK\$653.14 billion (If Exchange Fund Bills and Notes issued but not yet settled at end-November were excluded, the nominal value of Exchange Fund Bills and Notes would have increased by HK\$0.74 billion). Exchange Fund Bills and Notes issued include Exchange Fund Bills and Notes held as assets of the Exchange Fund.

5. In accordance with the accounting policies adopted by the Exchange Fund, Exchange Fund Bills and Notes issued on tender date but not yet settled are included in "Exchange Fund Bills and Notes issued". For the purpose of this Account, the corresponding accounts receivable are shown as deductions in arriving at the Monetary Base. There were no such receivables at 31 December 2010 (HK\$34,664 million at 30 November 2010).

6. This represents the net amount of receivable and payable for unsettled transactions of investments and redemption/issuance of Certificates of Indebtedness.

7. Starting from June 2001, Hong Kong dollar interest rate swaps have been used as a means to manage the cost of issuing Exchange Fund Notes. For the purpose of this Account, interest payable/(receivable) and revaluation losses/(gains) on these interest rate swaps are shown as a component of the Monetary Base and are included in "Net accounts (receivable)/payable". At 31 December 2010, there were interest receivable and revaluation gains amounting to HK\$29 million (HK\$67 million at 30 November 2010) and HK\$326 million (HK\$648 million at 30 November 2010) respectively.

8. It should be noted that the whole of the Exchange Fund assets, not just the Backing Assets, are available for the purpose of defending the linked exchange rate.