

## **Central Banking Publications**

### **2018 Lifetime Achievement Award**

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I am deeply honored by the conferment of the 2018 Central Banking Publications Lifetime Achievement Award. It is a great privilege to be chosen by the distinguished Awards Committee, a constellation of prominent economists and central bankers. I am blessed to have received this award one month before retirement, capping off my career with a final flourish. CBP has been a vital force in the realm of central banking. Its signature publication, the Central Banking Journal, is a must-read for serious central bankers in need of a solid grasp of the latest developments and new ideas in our profession.

This Lifetime Achievement Award is undoubtedly the greatest distinction that has been bestowed on me. It genuinely pains me that I am unable to express my gratitude here in person due to a very peculiar condition. My sincere apologies go to the CBP management for the inconvenience this has caused.

Twenty years and four days ago, I took office as the head of Taiwan's central bank – a formidable task at crunch time. The Asian financial crisis was wreaking havoc across the region, battering Southeast Asia before raging towards South Korea. The economies that were affected suffered massive capital outflows, precipitous declines in their currencies, liquidity shortage, sharp rises in interest rates, and deep recessions. The damage inflicted on Asian economies was so far reaching

that previous episodes could not serve as a useful guide. The crisis was in full swing when I took over the bank's official seal.

According to the classic tenets of central banking, the way to fend off such crisis is to allow the currency to depreciate and adopt a loose monetary stance. Back in 1998, unrelenting and massive capital outflows made it untenable to just follow the conventional wisdom because a weaker NT dollar would encourage yet more capital outflows. So much so that any monetary easing could not have eased the liquidity crunch. Apparently, the conventional treatment could not eradicate the woes because it addressed neither the symptoms nor the roots of the disease.

At that juncture, my own diagnosis was that the foreign exchange market was at the heart of the problem, one that could not be solved without stemming the tide of capital outflows. That's why the central bank took the decisive action to stop domestic corporations from trading NT dollar-linked non-delivery forwards, in effect closing the channel through which currency speculators had unlimited access to shorting the NT dollar. Taiwan's forex market subsequently stabilized and international capital outflows subsided. This paved the way for the adoption of an accommodating monetary policy, which in turn put the domestic economy back on its feet. We dished out the same prescription during the 2008-2009 global financial crisis when the central bank administered a potent policy mix to steady the forex market and safeguard the domestic financial system. Thanks to this approach, Taiwan was able to ride out the two devastating financial crises and emerged relatively unscathed.

For a highly-open small economy like Taiwan, monetary and exchange rate policies should be given equal weight, unlike larger

economies that can afford to focus primarily on monetary policy. I am sure most of you are familiar with the concept of Impossible Trinity in international economics. The trilemma has three components: a stable currency, free capital movement, and sovereign monetary policy, and the theory goes that a country can only achieve two of these policy objectives at the same time. Yet, for a small and highly-open economy like Taiwan having to pick just two out of three policy goals is not optimal. A better solution would be to adopt a managed floating exchange rate regime to keep exchange rates flexible and introduce appropriate capital flow management when necessary to ensure monetary policy remain effective. In short, we can choose an intermediate solution that can address all three policy objectives, albeit to a lesser extent, depending on economic and financial conditions.

During the past twenty years, I have been committed to fulfilling the legal mandates vested in me: to promote financial stability, guide sound banking operations, maintain the stability of the internal and external value of the currency, and foster economic development. Along the way, I have overseen the implementation of monetary and foreign exchange policy that steered Taiwan's economy safely through two international financial crises. But a central bank's mission goes beyond these headline grabbing feats. Away from the limelight, my colleagues modernized Taiwan's payment system, rolled out new loans to help earthquake victims and reformed the student loans programs. Together, we forestalled real estate bubbles with targeted macro-prudential measures, built a new foreign currency clearing platform, and promoted greater financial cooperation between the two sides of the Taiwan Strait. Over the years, Taiwan has also enjoyed a healthy balance of payments position,

continued expansion of foreign exchange reserves, and marked increases in net foreign assets held by the private sector. These distinctive features of the Taiwan economy do make the tasks of maintaining financial stability and fostering economic development a great deal easier than otherwise.

For those of you who are still awake, a few words of advice for achieving longevity in the central banking profession. Since I began my central banking career in 1971, I have been building knowledge through reading, carrying out statistical work, and gaining hands-on practical experience. I can still recall the days when I took charge of compiling the BOP statistics and the real effective exchange rate index. These seemingly dull and mundane number-crunching tasks can become powerful tools in understanding the finer points of economic and financial issues. For example, I have long recognized and made allowances for the intrinsic difference between the goods market and the foreign exchange market. While the forces of demand and supply would normally guide the goods market toward equilibrium, it is often not the case with the forex market. Take Taiwan for example. When foreign investors, who are prone to herding behavior, act collectively as a buyer of NT dollars, the supply curve of foreign exchange would shift to the right and the NT dollar appreciates significantly. In contrast, when foreign investors sell NT dollars in a joint move, the demand curve for foreign exchange would shift to the right and the NT dollar tumbles. Both scenarios often lead to exchange rate overshooting. As such misalignments cannot be explained by economic fundamentals, they can eventually morph into an economic crisis if left unattended to.

With this in mind, I wrote a paper in 1995 on the Mexican Peso Crisis that argued “Argentina, the Philippines, Indonesia, Thailand, and Saudi Arabia have been running current account deficits since 1987 and rely heavily on foreign capital inflows. Thailand, in particular, has witnessed more short-term capital inflows than other types. These signs spell cause for concern.” Two years later, unfortunately, the Asian financial crisis broke out and it did start with the collapse of the Thai baht.

Even avid reading cannot guarantee a true grasp of the wisdom to be found in great books. A deep understanding of the art of central banking requires more than reading. It takes years of hard work, dedication, and experience to be able to implement effective policies with speed and conviction when necessary. I was extremely lucky to have the loyal support of my colleagues, who have always acted with professionalism and integrity. It has been a pleasure and rare privilege to work alongside them.

Allow me to again express my deep gratitude to CBP for this wonderful award. This is not only a source of pride and inspiration for my colleagues and me, but also a worthy recognition for all the people in Taiwan. Thank you!