FOREIGN EXCHANGE TRADERS IN HONG KONG, TOKYO, AND SINGAPORE

A SURVEY STUDY

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ABSTRACT

This study presents some findings from a survey of interbank foreign exchange traders in Hong Kong, Tokyo, and Singapore regarding some issues in exchange rate economics. Exchange rates are perceived to react to the unexpected component of macroeconomic news within the first minute of announcements. On labeling their trading methods, the traders' responses distribute quite evenly among strategies based on technical and fundamental considerations. Central banks are accused of exacerbating volatility via intervention. While more than one-half of the traders suggest interventions restore equilibrium and are conducted at the right time, they are divided on whether interventions achieve their goal. Our survey results also indicate that the responses depend on the market in which the trader is located, seniority, trading capacity, market share, and headquarters location.

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INTRODUCTION

This paper reports some results from a mail survey of interbank foreign exchange traders regarding issues in exchange rate economics. The survey was conducted in the three major Far East foreign exchange markets; namely, Hong Kong, Singapore, and Tokyo. According to the Bank for International Settlements (1996), these three Far East centers account for 22.73 percent of the total global foreign exchange trading volume.

The survey methodology has been adopted to study economic phenomena for a long time. For example, one of the early survey studies is Hall and Hitch (1939). Since the recent float, a few survey studies on foreign exchange markets have been conducted. In the 1980s the Group of Thirty (1980, 1985) commissioned two survey studies on the global foreign exchange market. Recently, the Bank for International Settlements conducts a foreign exchange market survey once every three years. The survey focuses on transaction types and patterns in the major foreign exchange centers around the world. Results of the latest triennial survey were reported in the Bank for International Settlements (1996).

However, the survey approach is not unequivocally accepted by the profession. Economists' skepticism of the usefulness of survey studies can be traced back to the famous "billiard player" analogy (Friedman and Savage 1948). However, as argued by Blinder (1991), results from a properly designed survey can provide valuable complementary facts that are not otherwise available to economists. For example, the survey results in Taylor and Allen (1992) provide some interesting information on the use of technical analysis in the London foreign exchange market.[1]

The response of exchange rates to news releases is an issue considered in our survey. The asset price approach predicts that exchange rates, like other financial prices, react to information that alters expectations on fundamentals. Thus, effects of macroeconomic announcements, especially the unexpected component, can provide useful insights on the effects of fundamentals on exchange rates. Our survey draws on the first-hand experience of the traders and solicits their views on the rate at which exchange rates react to the unexpected component of macroeconomic announcements.

Foreign exchange dealers in the major trading banks jointly determine the interbank foreign exchange rates. Their trading activity thus has profound implications for exchange rates. However, there is limited empirical evidence on the trading strategies pursued by interbank foreign exchange traders. One set of our survey questions is designed to gather information on trading behavior. Specifically, we provide the traders with a list of trading strategies and ask them to select one strategy from the list to label their trading methods.

Central bank intervention is a well-publicized event in the global foreign exchange market. Central banks intervene in the market when they decide exchange rates have substantially deviated from their equilibrium values, a situation typically attributed to speculative activity though monetary and economic policies can well be the explanation. In general, the desirability of official intervention depends on the motivation. Even Milton Friedman (1953) consents to official intervention if the objective is to smooth out temporary fluctuations and not to interfere with fundamental adjustments. Foreign exchange dealers are frontline players in the interbank market and directly observe the impact of central bank intervention. In this survey study the market practitioners are asked to assess the effects of intervention.

In this survey we have replies from traders with diverse backgrounds from three different foreign exchange centers. The sample offers an excellent opportunity to determine if traders have different views of the market and if the response patterns

Table 1. Information About Respondents and Their Organizations

	1.a Respondent's Position		
	Hong Kong	*Tokyo*	*Singapore*
Treasurer/Manager	68	28	30
Chief/Senior Dealer	117	38	44
Dealer/Junior Dealer	37	9	7
Others	5	1	8
Total	227	76	89
	1.b Daytime Position Limit (Million US$)		
	Hong Kong	*Tokyo*	*Singapore*
Below 10	31.5%	25.7%	15.2%
10-25	36.0%	13.5%	26.6%
26-40	10.0%	12.2%	15.2%
41-55	4.5%	12.2%	16.5%
56-70	2.5%	8.1%	2.5%
over 70	12.0%	27.0%	19.0%
Value at Risk	3.5%	1.4%	5.1%
	1.c Headquarters Location		
	Hong Kong	*Tokyo*	*Singapore*
North America	17.6%	13.2%	27.0%
Europe (include UK)	44.5%	26.3%	29.2%
Asia	33.5%	50.0%	32.6%
Others	4.4%	10.5%	11.2%
	1.d Average Daily Turnover of the Organization (Million US$)		
	Hong Kong	*Tokyo*	*Singapore*
Below 100	40.7%	36.8%	23.7%
100-500	27.3%	33.8%	32.9%
500-1000	9.3%	8.8%	22.4%
Over 1000	22.7%	20.6%	21.1%

Note: Panel 1.a reports the number of respondents under each of the listed job capacities. Other panels present the percentages of respondents who selected the listed choices. For some questions, the component frequencies of a category do not sum to one due to rounding. In some cases there are multiple responses or incomplete replies.

depend on some characteristics of the respondents. Findings of heterogeneous perceptions and behavior among traders will lend strong support to the use of a heterogeneous agent model in the exchange rate literature.

The rest of the paper is organized as follows. The next section briefly describes the survey and some preliminary data about the respondents. The third section reports the respondents' views on the adjustment to the unexpected component of macroeconomic announcements, the best way to label their trading strategies, and effects of intervention. The fourth section investigates if the response patterns depend on market location, turnover volume, location of headquarters, seniority, and trading capacity. Some concluding remarks are offered in the final section.

SURVEY DESIGN AND PRELIMINARY RESULTS

In preparing the questionnaire we incorporated advice, comments, and suggestions of a few prominent market practitioners. The survey was conducted between October 1995 and January 1996. In total, 1,961 questionnaires were sent to bank dealers in the Hong Kong, Tokyo, and Singapore interbank foreign exchange markets.[2] The mailing list was prepared from the Dealers Directory published by the Hambros Bank and information provided by the Forex associations in these three regions. We received 392 copies of the completed questionnaire. The response rates were 32.15 percent from Hong Kong, 14.42 percent from Tokyo, and 13.82 percent from Singapore. These response rates are quite reasonable for a mail survey (Alreck and Settle 1985, p. 45). Copies of the survey are available from the authors.

Information about the respondents and their organizations is summarized in Table 1. Judged by the responses reported in panel 1.a, most of the respondents are experienced traders in the foreign exchange business. Over 80 percent have the title of "chief/senior dealer" or "treasurer/manager."[3] The pattern of responses roughly matches the distribution of trader's seniority in the mailing list. We use a nonparametric test of homogeneity to evaluate the hypothesis that the three markets have the same proportion of respondents in each of the four listed positions.[4] The test gives a chi-square statistic of 6.0, which has a p-value equal to 0.40. This means the distributions of the respondents' seniority are not significantly different in these three foreign exchange centers.

The intraday position limit is the maximum open position a dealer is authorized to assume during the day. Since, in most cases, dealers square their positions at the end of a trading day, the intraday position limit can be used as a proxy for a dealer's trading capacity.[5] The position limits of our respondents exhibit a bimodal distribution (panel 1.b). Most respondents have a daytime position limit either below US$40 million or above US$70 million even though responses from the Tokyo market spread more evenly across different position limit classifications. The test of homogeneity yields a statistic of 30.5 (p-value = 0.00) which indicates