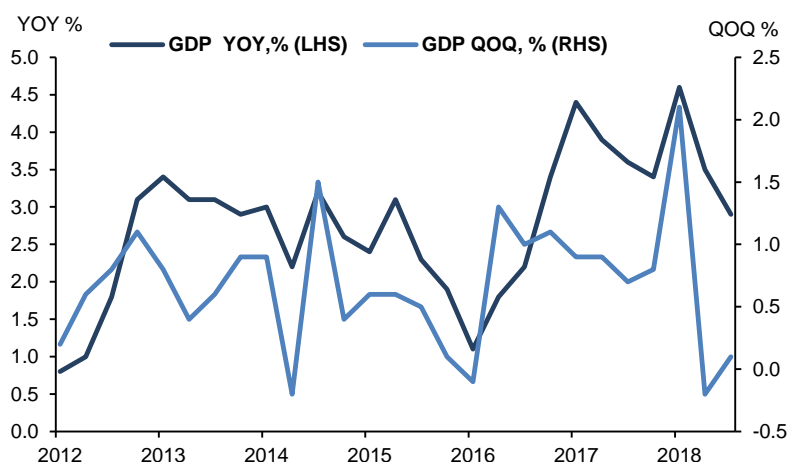


Global Markets Research
Economics – Hong Kong

3Q GDP growth eased to 2.9% YOY

The Hong Kong economy expanded a modest 2.9% YOY in the third quarter of 2018 extending from the normalization in 2Q. While coming below consensus estimate, the lower showing matched general expectations that growth in the Hong Kong economy is moderating further against a backdrop of rising trade protectionism given its over reliance on demand from Mainland China. We continued to believe that a slower external trade sector will spill over into domestic economy weighing on household consumptions in particular thus leading to more moderate growth in the near term.

Figure 1: Hong Kong GDP Growth



Source: Censtatd, Bloomberg

GDP growth eased to the slowest since 3Q2016

Hong Kong real GDP growth tapered off further to 2.9% YOY extending from the normalization in the second quarter (2Q: +3.5%). The sharp pullback in growth was more than expected and was the slowest recorded since 3Q2016. On a quarter-on-quarter seasonally adjusted basis, the economy rose a mere 0.1% QOQ (1Q: -0.2%).

Slower spending masked growth in public investment

Private consumption expenditures eased further inching up 5.2% YOY in 3Q (2Q: +6.0%) amidst weaker spending in food, consumers goods and services. Investment recorded an impressive growth of 8.2% YOY (2Q: +1.1%) mainly driven by the astounding increase in investment in machinery, equipment, and intellectual property products (+24.1% vs +4.9%) on lower base effect.

Net exports dragged down overall growth due to high base effect.

While compared to the previous quarter, exports growth eased only slightly to 4.7% YOY (2Q: +4.8%) as the faster growth in goods shipment (+50% vs +4.6%) was offset by the slower services exports (+3.1% vs +5.9%). Imports meanwhile increased 7.0% YOY (2Q:+5.5%), the fastest pace since 1Q17. An annual contraction in net exports (-85.2% vs -38.7%) due to the higher base effect serves as a drag on overall growth.

Still-steady exports momentum in 3Q likely to be temporary

The still-steady exports growth in 3Q was supported by Chinese firms' ramping up purchases from Hong Kong as they rushed out shipments to the US in that time period to avoid further tariffs. Despite slower exports growth to China in September, we think that the still-steady momentum could be sustained towards the end of the year with more pronounced drop likely happening in the beginning of 2019.

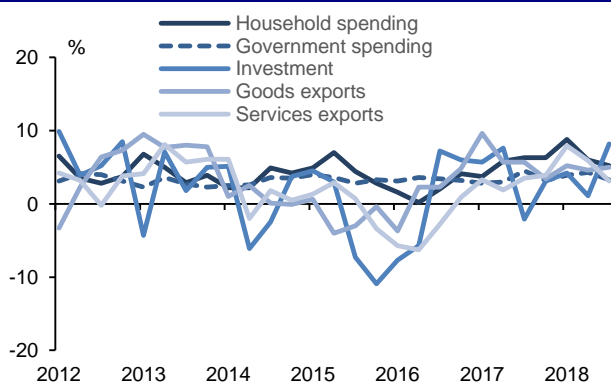
A combination of various factors to drag down domestic economy

External headwinds are likely to spill over into the domestic economy leading to weaker private consumption. Lesser demand in the trade sector means that wage earners at the city's massive port hub could be out of job soon resulting in subdued wage growth. Falling stock prices since the start of the year (the Hang Seng Index has erased nearly 14% YTD) meanwhile weighs down household wealth. Both factors are set to dampen household spending. The impressive growth in monthly visitor arrivals this far this year is also likely to trend down next year (Chinese visitor arrivals are projected to slow) and retail sales would crimp.

Given its over reliance on mainland Chinese demand, we reaffirm our view that growth is moderating in Hong Kong due to a combination of external and domestic challenges. The Hong Kong government has thus refined its 2018 growth forecast from 3-4% to 3.2% YOY.

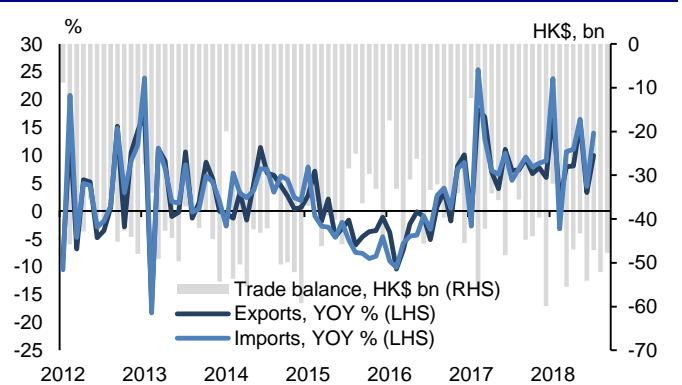
Hong Kong Overview:

Figure 2: GDP Expenditure Components



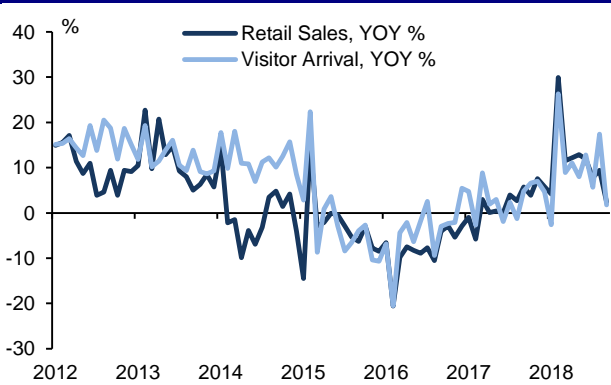
Source: Censtatd, Bloomberg

Figure 3: External Trade



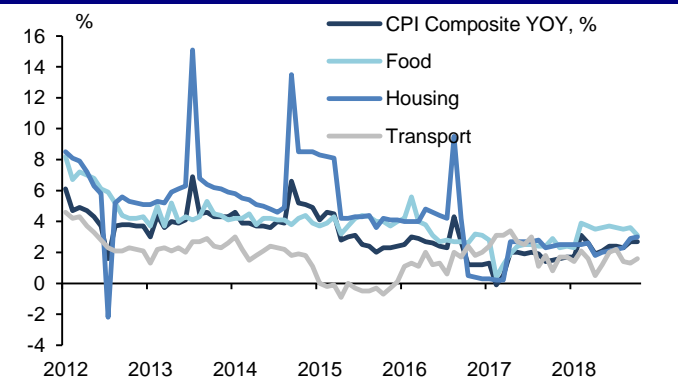
Source: Bloomberg

Figure 4: Retail Sales and Visitor Arrival



Source: Bloomberg

Figure 5: CPI and Major Components



Source: Bloomberg

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