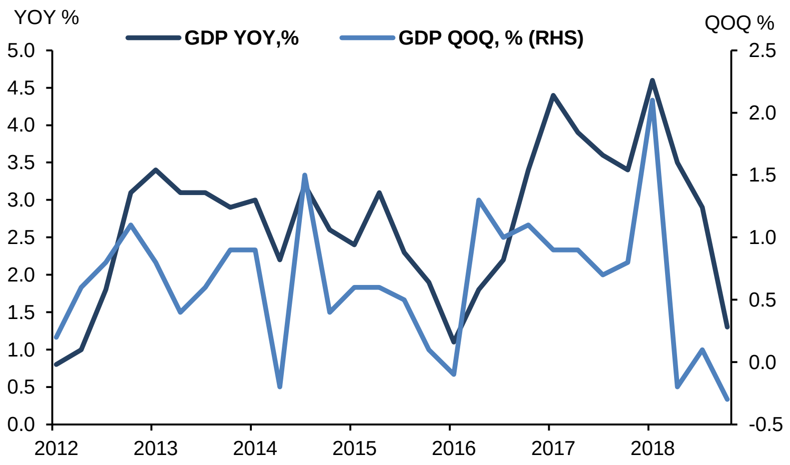
4Q GDP growth weakened to near 3-year low

Hong Kong 4Q GDP growth turned out to be a huge disappointment, easing to a mere 1.3% YOY from the 2.9% YOY in the third quarter of 2018. The much weaker showing came well below consensus estimate of 2.2% YOY, suggesting that the impact of China's slower growth, a slowing property sector and weakening domestic consumptions on the local economy was more pronounced than expected. Outlook for the Special Administration Region (SAR)'s growth trajectory remains skewed to the downside amidst a soft global economic condition, particularly that of China. Upsides to the economy include potential rebound in its property sector and a successfully negotiated trade deal between the US and China.

Figure 1: Hong Kong GDP Growth



Source: Censtatd, Bloomberg

GDP growth decelerated to slowest level since 1Q16

Hong Kong real GDP growth decelerated further to 1.3% YOY in the fourth quarter of 2018 (3Q: +2.8% revised). The bigger than expected pullback in growth was a major disappointment, coming well below a Bloomberg consensus estimate of 2.2% YOY, and was the slowest recorded rate since 1Q16, effectively dragging down 2018 full-year real GDP growth to 3.0% (2017: +3.8%). On a quarter-on-quarter seasonally adjusted basis, GDP fell by 0.3% QOQ (3Q: +0.1%) after posting a mere 0.1% gain in the previous quarter.

Slower private consumption outweighed stronger government expenditure

Growth in private consumption expenditures maintained its downward trend, softening to 3.1% YOY in 4Q (3Q: +4.8% revised) driven by a fall in spending on food (-0.6% vs +0.9%) as well as the slower gains in spending on consumer goods (+5.8% vs+10.0%) and (+2.5% vs +3.2%). This was largely in line with the poor performance of retail sales, as consumers tightened spending in the last few months of 2018. The increase in government consumption expenditures however was the strongest since 1Q04, rising by 5.0% YOY (3Q: +3.3%) reflecting the government's higher investment particularly in the tech sector.

Investment in construction fell, reflecting slower property sector

Investment fell for the first time since 3Q17 by 5.4% YOY (3Q: +9.2%) after recording an impressive growth in the previous quarter largely reflecting the contraction in building and construction investment (-6.0% vs +1.1%) as the property sector slowed in 2H18. Growth in machinery, equipment and intellectual property products (+4.6% vs +21.0%) also came off from the elevated level in 3Q.

Trade sector weakened on soft global demand, especially China

Plague by softer global demand, total exports eked out a tiny gain of 0.2% YOY (3Q: +4.8%), after a few solid quarters. Exports of goods fell for the first time since 1Q16 by 0.2% YOY (3Q: +5.0%) after maintaining around 5% growth for the first three quarters. Services exports growth meanwhile eased to 2.9% YOY (3Q: +3.4%), continuing its downward trend since 1Q18.

Similarly, total imports dropped 0.5% YOY (3Q: +7.1%), the first time since 1Q16 as well largely on the decline in imports of goods (-0.8% vs +7.7%). Services imports also increased at a slower rate (+2.0% vs +2.5%), suggesting weaker domestic demand in general.

Outlook remains dismal, upsides to economy include rebound in property sector and US-China trade deal.

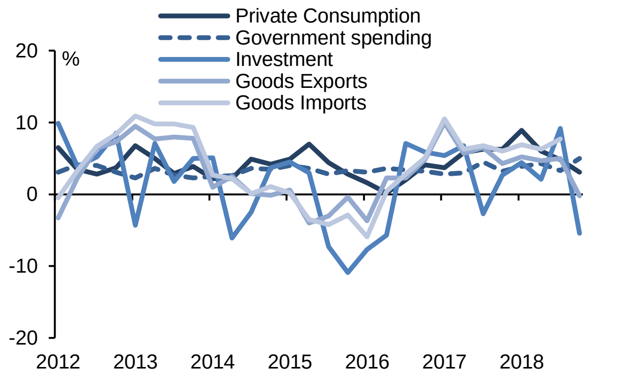
The slower GDP growth was in tandem with the general slowdown of 4Q GDP growth across developed economies as well as China, considering the fact that the SAR relies heavily on the Mainland for the growth of its trade sector, while the performance of its retail sector was also partly affected by Chinese visitors' spending in the domestic market. The softer real estate sector in 2018 meanwhile weighed down on household wealth in general, leading consumers to spend on a much cautious mode last year.

We maintain a bearish outlook for the economy in the near term as outlook for the global economy remains skewed to the downside. Headwinds at the manufacturing sector will continue to weigh down on Chinese economic growth, Japan's 4Q revival was unsustainable, Eurozone growth likely to remain tepid before Germany's car sector rebounds in 2H, while growth in the US is poised to soften on waning fiscal stimulus effect. Yesterday's trade report also witnessed the second consecutive month of decline in total exports, albeit at a slower pace mainly because of a less pronounced fall in shipments to China ahead of the Lunar New Year in early February.

Upside to the economy is the potential rebound in property prices as the surge in agreed sales and transaction values offered tentative signs that demand is returning to the sector (among the most unaffordable markets in the world) amidst dovish interest rates expectations. Investors are now expecting slower pace if not fewer rate hikes by the Fed – HKMA monetary policy moves in tandem with the Fed's as the currency is pegged to the dollar- which is likely to keep interest rates subdued, hence lower financing cost for homes in Hong Kong. Positive development at the trade front will undoubtedly be beneficial to Hong Kong as China and the US seem getting nearer to a deal.

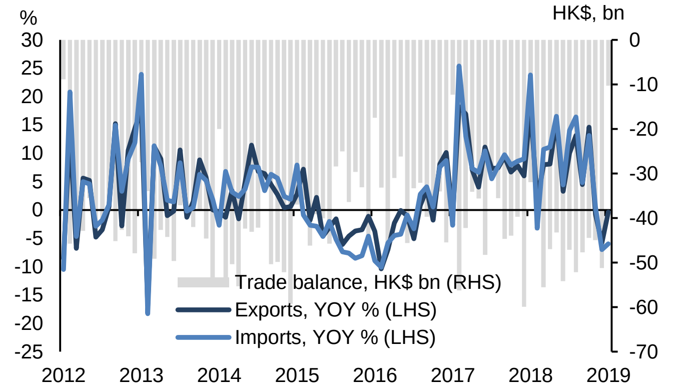
Hong Kong Overview:

Figure 2: GDP Expenditure Components



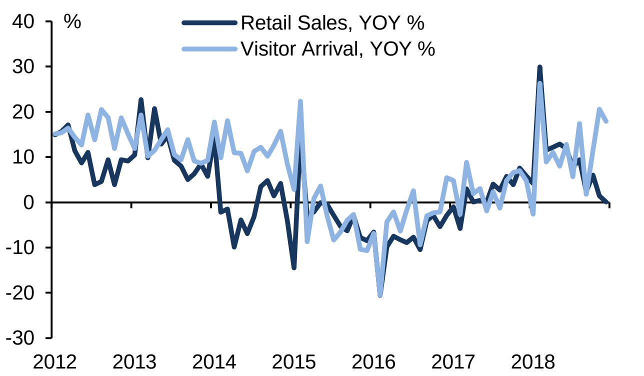
Source: Censtatd, Bloomberg

Figure 3: External Trade



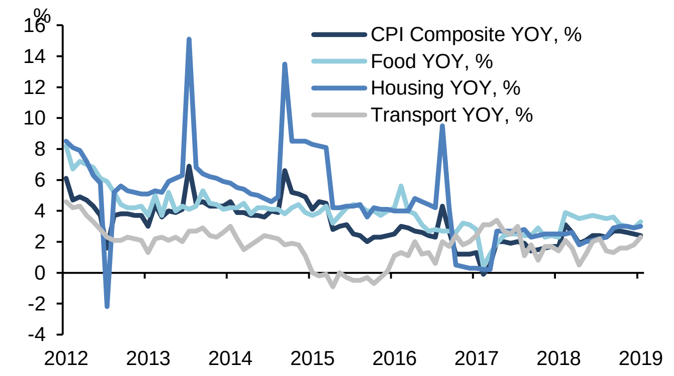
Source: Bloomberg

Figure 4: Retail Sales and Visitor Arrival



Source: Bloomberg

Figure 5: CPI and Major Components



Source: Bloomberg

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