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Global Markets Research

Research Alert

Hong Kong economy shrank 6.1% in 2020

- **Worst annual contraction on record**
- **High unemployment rate remains a concern**
- **Stronger external demand a positive sign for trade related sectors**

Background

The Hong Kong economy contracted by 3.0% y/y in the final quarter of 2020, an improvement from the 3.6% decline in the third quarter thanks to improvement in domestic and external demand. On a seasonally adjusted quarter-on-quarter basis, GDP posted a minor 0.2% expansion, compared to the 2.7% q/q growth prior, reflecting the economic impact of Covid-19 restrictions placed on 10 December. For the full year of 2020, the economy shrank by 6.1% (2019: -1.2%), marking its second year of downturn and also its largest ever contraction.

Compared to the same quarter last year, improvements were broad-based. Personal consumption expenditure fell 7.2% y/y (3Q: -8.2%); government spending reported a more modest 5.6% y/y growth (3Q: +7.1%). Domestic investment turned around and grew 2.6% y/y (3Q: -10.9%). Exports of goods rose 5.5% (3Q: +3.9%) while exports of services declined 29.3% (3Q: -33.5%) with the tourism sector still battered by the absence of foreign travellers. Goods imports picked up sharply by 6.9% (3Q: +1.9%) while services imports remained nearly 36% lower (3Q: -36%).

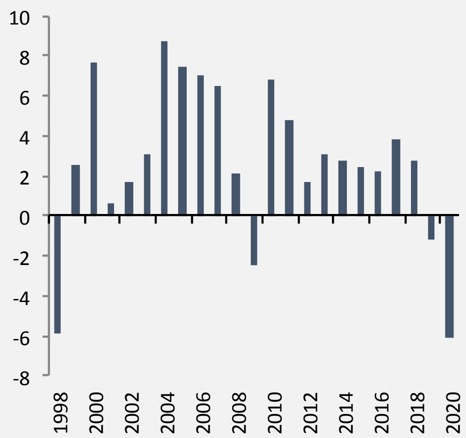
Outlook

We expect consumer demand to continue improve in 2021 although it is unlikely to see a marked increase in spending judging from the elevated level of unemployment rate (7.0% in January) and the continuously weak property prices.

The government's undaunted commitment to contain the pandemic via strict social distancing rules could constrain overall economic activity, thus limiting growth potentials. This is evident in the meagre quarterly growth in 4Q when the government significantly tightened rules on 10 December and made several extension thereafter. These swift responses have proven to be effective thus far, keeping daily cases at low levels. Restrictions have been loosened for the Feb 18 -March 3 period. This shall lead to some temporary boost to overall consumption but any spike in cases (followed by tighter rules) would risk reversing any gains.

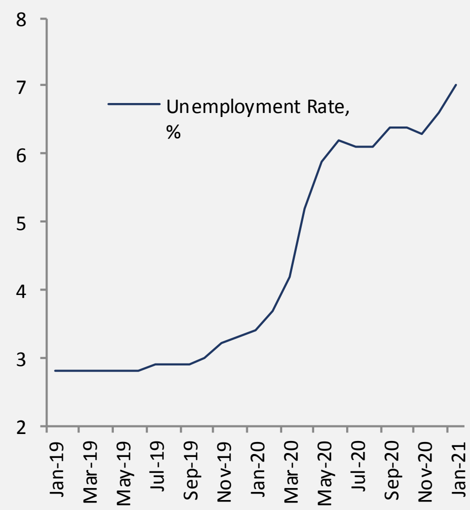
International travel is expected to remain shuttered for the rest of the year with the WHO now expecting the pandemic to end in early 2022. Visitors from China which are crucial for Hong Kong's retail sector remained extremely low. The 21-day hotel quarantine requirement (for visitors outside China) also serves as deterrence.

Figure 1: Hong Kong's economy contracted for second year in a row



Source: Bloomberg

Figure 2: Unemployment Rate remained high despite economic recovery



Source: Bloomberg

Having said that, Hong Kong is expected to continue benefit from strong external demand particularly from China via the trade sector. Exports to China surged nearly 18% at late 2020 while exports to other trading partners also recorded a modest increase for the second consecutive month. Rising global vaccination rate and easing infections in major countries suggest that global demand could pick up further in the coming months.

Government pledged HKD120b to fight pandemic downturn

The government announced this morning that it has pledged over HKD 120b ($15.5b) worth of funds for counter cyclical measures designed to combat the pandemic-related downturn. This is part of a HKD727.8b spending plan for financial year 2021-22. Among the measures include HKD5000 electronic vouchers to each resident to encourage spending as well as an ear-marked HKD15b in guaranteed personal loans for the jobless. The overall budget is expected to have a stimulus effect of around 2.0% of GDP and the government is expected to incur a budget deficit of HKD101.6 in the 21-22 financial period, compared to the HKD 257.6b deficit in 20-21. Historically it had been able to maintain a fiscal surplus but the US-China trade war and domestic unrests in 2018-2019 brought an end to the 15-year streak. In a bid to narrow the fiscal gap, it resorts to raise revenues by hiking the trading tax from 0.1% to 0.13%. It has also embarked on an expenditure reduction program to cut spending across bureaucracies. The government estimated that the economy would grow 3.5 to 5.5% in 2021.

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