15 May 2023

Global Markets Research

Research Alert

Hong Kong GDP grew by 2.7% in 1Q

1Q GDP ended 4 quarters of contractions on robust consumer spending

Consumption supported by removal of COVID restrictions and border control

Triple risks of global economic slowdown, higher inflation and interest rates

Overview

Hong Kong's GDP rebounded more than expected to +2.7% y/y in 1Q (4Q: -4.1% y/y), ending four consecutive quarters of declines. Private consumption was the biggest contributor to growth, surging by 13.0% y/y (4Q: +1.7% y/y), while exports continued to decline, mainly due to goods. Exports of services, on the other hand, rose significantly by 20.4% y/y (4Q: +1.2% y/y), due to revival of tourism activities.

Consumer spending and travel boost

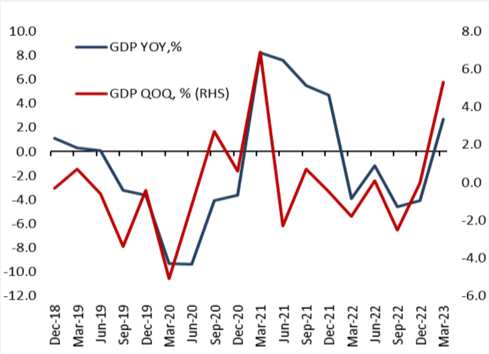
Looking ahead, latest indicators continued to suggest that this positive trend will continue at least in 2Q but with concerns over tightened financial conditions. In fact, Hong Kong Chief Executive John Lee expects Hong Kong's 2Q economic growth to outpace 1Q, with inbound tourism and domestic demand to remain the major drivers of growth. Retail sales expanded by a notable 40.9% y/y in March (Feb: +31.3% y/y vs. Jan: +6.9% y/y) as domestic demand remained firm with the return to normalcy, extension of consumption vouchers as well as favourable labour market. Unemployment rate fell more than expected to 3.1% for the three months ended March (Feb: 3.3%) with the unemployment rate for consumption- and tourism-related sectors falling 0.1ppts to 4.2% during the period.

On the external front, the jump in export of services suggests that the resumption of inbound travel has benefitted consumer spending. As it is, tourist arrivals jumped to 4.4m in 1Q (1Q22: 0.01m) with 76.1% of the tourist arrivals from mainland China. With forward looking China's services PMI still high at 56.4 in April (March: 58.2), this suggests that land travel may will stay robust, especially in lieu of the Golden Week in May,

External demand

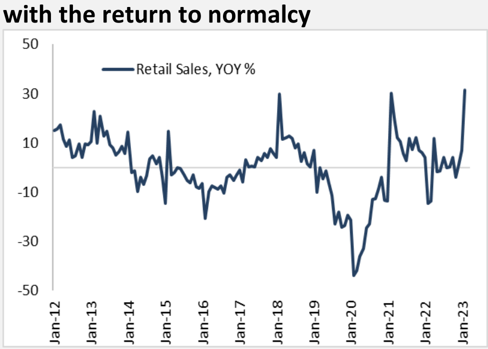
In our view, a recovery in exports of goods will be challenging at this juncture. Hong Kong's exports unexpectedly contracted 1.5% y/y in March (Feb: -8.8% y/y), with exports to China continued to fall despite the removal of restrictions for cross-boundary truck movement. With slower growth in advanced economies to continue to weigh on demand, pinning hopes of China, which accounts for 50-60% of Hong Kong's monthly exports, will be a tall order if China's official manufacturing PMI is any indication. The index hit its lowest level since post-Covid reopening, unexpectedly dipping below to 49.2 in April (March: 51.9).

Figure 1: First quarterly expansion since 2021



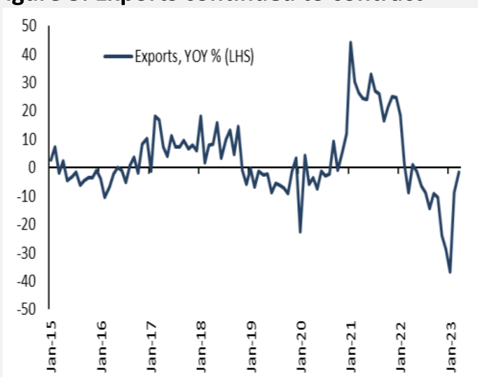
Source: Bloomberg

Figure 2: Retail sales growth has picked up with the return to normalcy



Source: Bloomberg

Figure 3: Exports continued to contract



Source: Bloomberg

Recovery in business sentiment

Nevertheless, business sentiment among large enterprises has improved and is expected to improve across. According to the latest government survey, the proportion of respondents expecting better business situation increased to 25% in 2Q (1Q: 19%), led by the accommodation and food services, manufacturing, retail and financing and insurance sectors. Notwithstanding the uncertainties due to tight financial conditions, this should bode well for private investment going forward. As it is, gross domestic fixed capital formation has already rebounded to chart positive growth of +5.8% y/y in 1Q (4Q: -8.9% y/y).

Inflation rate will increase on improved domestic activities

Hong Kong's underlying CPI held steady at +1.7% y/y in March when compared to February, but is a sharp deceleration from +2.1% for the period Jan-Feb as food prices softened sharply due to high base effect. Prices of energy-related items, clothing and footwear as well as meals out and takeaway food, on the other hand, accelerated further, suggesting domestic cost pressure in view improved domestic activities.

Companies will also have to readjust to higher costs, especially in view of a slew of price hikes announced and anticipated. Electricity tariffs were revised upward by 5.0% in March, Star Ferry ticket prices jumped more than 50% in April, train fares may increase 2.3% this year, bus operators have pushed for fare increases of up to 50%, while the Government has proposed to double the toll for Cross-Harbour Tunnel and Eastern Harbour Tunnel in August.

Capping this will be some moderation in food prices with the reopening of land border as well as diversified food supply. China currently supplies 42.2% of Hong Kong's good supplies, followed by Taiwan and Singapore.

Outlook

Taking into account the 1Q GDP, the government maintained its full year GDP forecast for 2023 at 3.5%-5.5%, with growth likely be near the upper bound of the range. Growth will continue to be domestic driven, supported by a return to normalcy in terms of economic activities, disbursement of consumption vouchers under Budget 2023, favourable labour market as well as inbound tourism. Growth will however, be negated by tightened financial conditions, as well as expectations of still slow external demand in view of still shaky recovery for China's economy as well as uncertainties in global economic outlook.

Figure 4: Inflation has remained tame at this juncture, but will increase

Source: Bloomberg

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