

# HONG KONG ECONOMIC MONITOR

Treasury Division



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May 2009

## Hong Kong Economy: Less Bad, but Not Good Enough

Better news on unemployment, exports and retail sales seem to suggest that the economic downturn might be bottoming.

March unemployment rate rose 0.2 percentage point from the previous month, compared to a 0.4 percentage point increase in February. Hong Kong's total exports decreased 21.1% in March, slightly better than the 23.0% contraction recorded in the previous month. March retail sales dropped 9.3% in volume, compared to a 13.9% decline in February.

The data may be less bad, but they are not good. Economic and trading activities remain in contraction mode, although the pace of contraction seems to be less severe.

The recent outbreak of the influenza A (H1N1) also warrants close monitoring. Further spreading of the flu could submerge the "green shoots" that are springing up in the global economy, leading to a gloomier outlook for the highly trade-dependent Hong Kong economy.

**Exhibit 1: Hong Kong's Economic Forecast**

| (% yoy changes)     | 2008 | 2009F |
|---------------------|------|-------|
| Real GDP            | 2.5  | -3.0  |
| Consumer prices     | 4.3  | 1.0   |
| Unemployment*       | 3.6  | 6.3   |
| Export value        | 5.1  | -7.5  |
| Retail sales volume | 5.0  | -8.0  |

Note: \* average for the year; (F) forecast.

Sources: Hong Kong's Census and Statistics Department, Hang Seng Bank



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## Retail Sales Continue to Fall

Retail sales volume dropped 9.3%<sup>1</sup> in March, after declining 13.9% in February. However, the smaller contraction does not imply an improving trend as readings in the first two months were distorted by the timing of the Lunar New Year holidays. Taking the first two months' data together, retail sales volume fell 3.6%.

The fall in consumer demand was broadly based. Sales of clothing and footwear, consumer durables and other consumer goods declined 17.5%, 11.5% and 10.0% respectively. Jewellery, watches and clocks items, which target mostly tourists, also recorded double-digit declines.

Exhibit 2

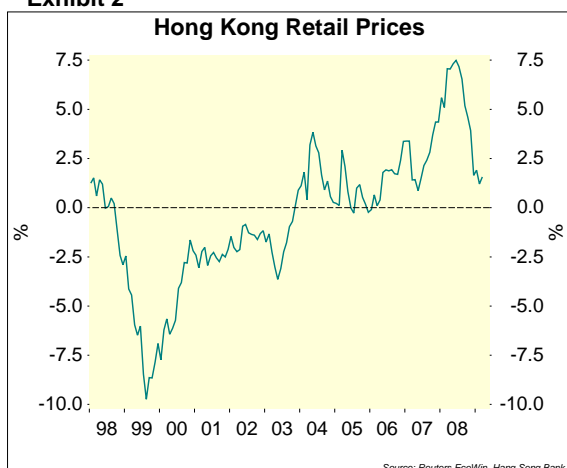


Exhibit 3

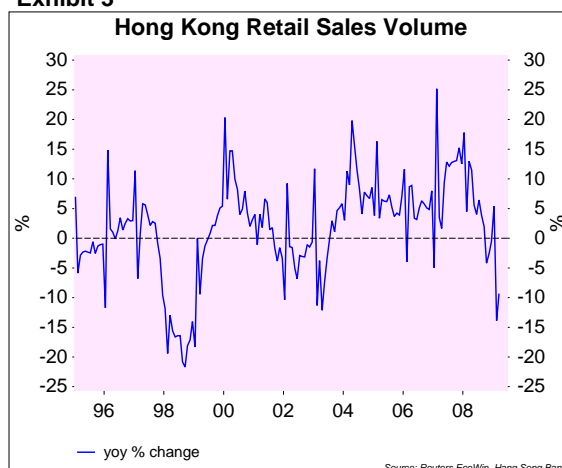


Exhibit 4: Hong Kong Retail Sales Volume

| (%)   | Feb 09       | Mar 09      |
|---|--------------|-------------|
| <b>All retail outlet</b>                    | <b>-13.8</b> | <b>-9.3</b> |
| Food, alcoholic drinks & tobacco            | -8.9         | -2.5        |
| Supermarket                                 | -17.2        | -3.6        |
| Fuel  | 3.7          | 4.6         |
| Clothing & footwear                         | -23.7        | -17.5       |
| Consumer durables                           | -10.0        | -11.5       |
| Department stores                           | -24.3        | -7.9        |
| Jewellery, watches, clocks & valuable gifts | -6.5         | -9.7        |
| Other consumer goods                        | -10.4        | -10.0       |

Source: Hong Kong's Census and Statistics Department

Looking ahead, business conditions for retailers are likely to remain unfavorable. Rising unemployment and falling income would continue to undermine consumer confidence.

<sup>1</sup> Changes throughout the report are on year-on-year basis unless otherwise stated.



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The recent outbreak of the influenza A (H1N1) is to watch, which is likely to be a double blow to the retail business. We expect retail sales volume to decline 8.0% for the whole of 2009 and see risk to the downside.

## Less Severe Contraction in Exports

Hong Kong's total exports decreased 21.1% in March, after falling 23.0% in the previous month.

Recent economic reports in our major export markets seem to show early signs of stabilization. The latest leading economic indicators in the US and Europe, as measured by purchasing managers' indices (PMIs), rebounded from low levels. However, it is too early to be too optimistic. While the PMIs might have stabilized, they remain below the threshold of 50, indicating a contraction in manufacturing activities. In addition, consumers in these markets still have to contend with shrinking wealth and rising unemployment and therefore look unlikely to substantially increase spending anytime soon.

The recent outbreak of the influenza A (H1N1) also poses risks to the fragile global economy, clouding the outlook for Hong Kong's exports.

We expect total exports to fall by 7.5% in 2009 in nominal terms, but see substantial risk to the downside.

Exhibit 5

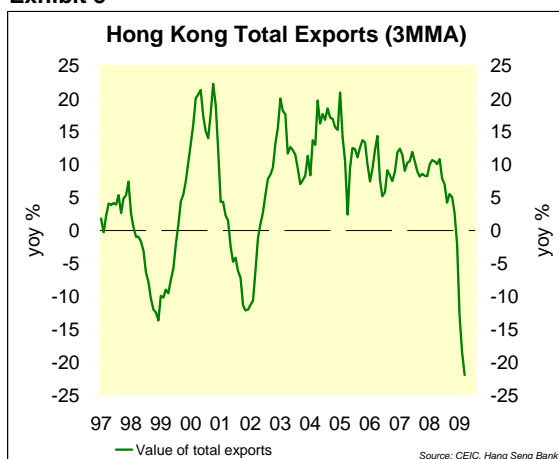


Exhibit 6

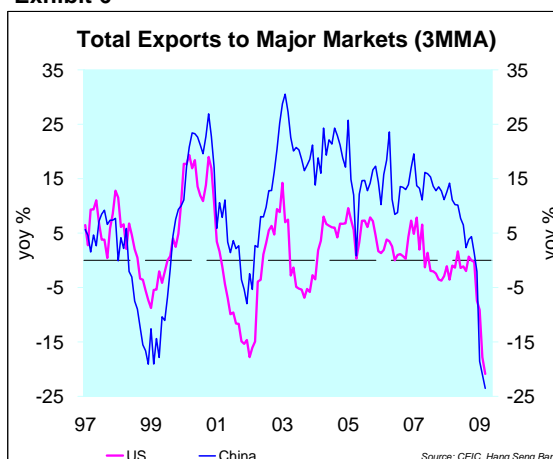


Exhibit 7: Hong Kong Trade Statistics

|                  | Feb09  | Mar09  |
|------------------|--------|--------|
| Total exports    | -23.0% | -21.1% |
| Domestic exports | -39.6% | -41.1% |
| Re-exports       | -22.4% | -20.5% |
| Imports          | -17.5% | -22.7% |

Source: Hong Kong's Census and Statistics Department



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## Unemployment Rate Rises at Slower Pace

Hong Kong's unemployment rate rose to 5.2% in March, the highest since November 2005.

Total employment dropped to 3.51 million, as 5,500 jobs were lost in March. The number of unemployed persons continued to rise, reaching 187,200. Among the major industry sectors, the increase in the unemployment rate was most notable in imports and exports trade and the transportation sectors.

The pace of increase seems to have slowed. March unemployment rate gained 0.2 percentage point from the previous month, compared to a 0.4 percentage point increase in February.

But the labour market is likely to continue to be under pressure, as the economic environment remains tough. Employment prospects are dim in the near-term. The unemployment rate is expected to climb further, reaching a peak of about 7%. For 2009 as a whole, the unemployment rate would average 6.3%.

Exhibit 8



Exhibit 9

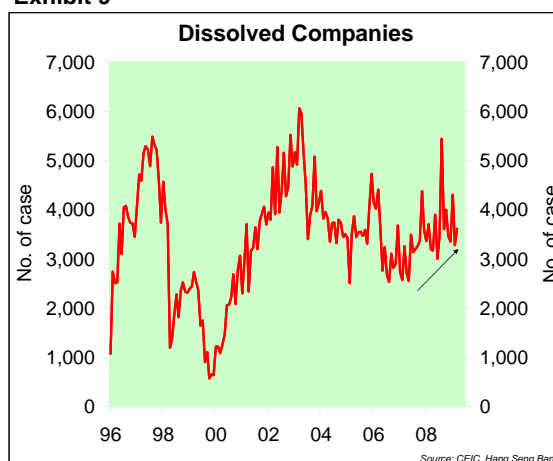


Exhibit 10: Unemployment Rate % (Major Industry)

|       | Import & export trade | Real estate & business services | Education & medical services | Wholesale & retail | Transport |
|-------|-----------------------|---------------------------------|------------------------------|--------------------|-----------|
| Oct08 | 2.7                   | 2.5                             | 1.4                          | 4.9                | 3.4       |
| Nov08 | 3.0                   | 2.7                             | 1.4                          | 5.3                | 3.5       |
| Dec08 | 3.3                   | 2.7                             | 1.6                          | 4.9                | 3.8       |
| Jan09 | 3.9                   | 3.4                             | 1.9                          | 5.2                | 4.5       |
| Feb09 | 4.3                   | 3.5                             | 1.7                          | 5.1                | 5.3       |

Source: CEIC





## Inflation Edges Up

March consumer price inflation rose to 1.2%, from 0.8% in February. It does not imply inflation has reversed course, as the drop in February inflation was aggravated by the timing of the Lunar New Year holidays. Taking the two months together to neutralise the seasonal effects, consumer price inflation was 2.0%.

The reading was also affected by the government's one-off relief measures. For instance, the electricity subsidies led to a 42.9% plunge in utilities prices. Netting out the impact of these special factors, the underlying inflation was 2.6%, notably lower than the 3.3% registered for the first two months.

Exhibit 11

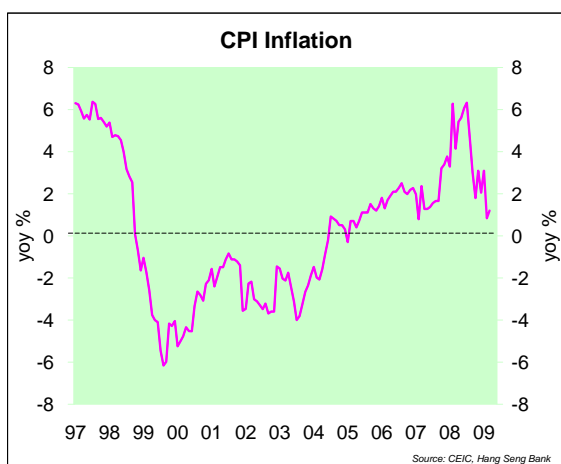


Exhibit 12: Hong Kong Composite CPI Component, yoy %

|                                     | Feb09 | Mar09 |
|-------------------------------------|-------|-------|
| <b>All items</b>                    | 0.8   | 1.2   |
| Food                                | 3.0   | 3.8   |
| Meals bought away from home         | 3.0   | 2.7   |
| Exclude meals bought away from home | 3.1   | 5.4   |
| Housing                             | 6.9   | 5.4   |
| Electricity, gas & water            | -43.1 | -42.9 |
| Alcoholic drinks & tobacco          | 1.8   | 22.2  |
| Clothing & footwear                 | 1.4   | 4.3   |
| Durable goods                       | -3.0  | -2.5  |
| Miscellaneous goods                 | 3.2   | 2.3   |
| Transport                           | 0.4   | 0.1   |
| Miscellaneous services              | -4.0  | -2.5  |

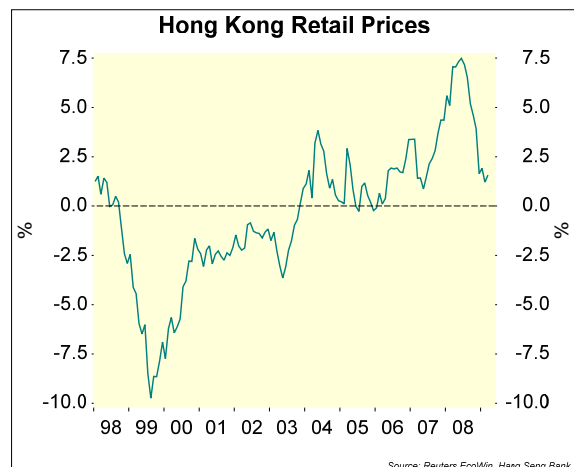
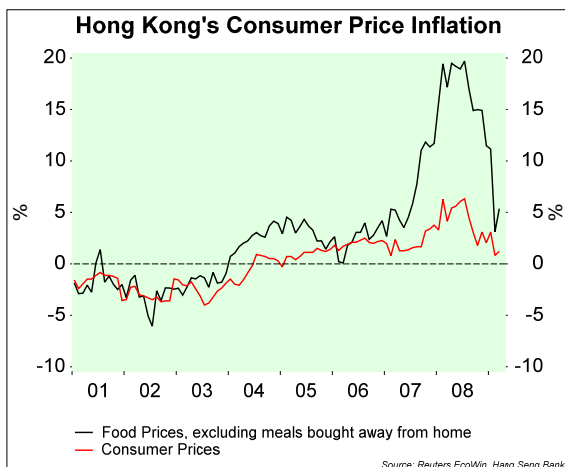
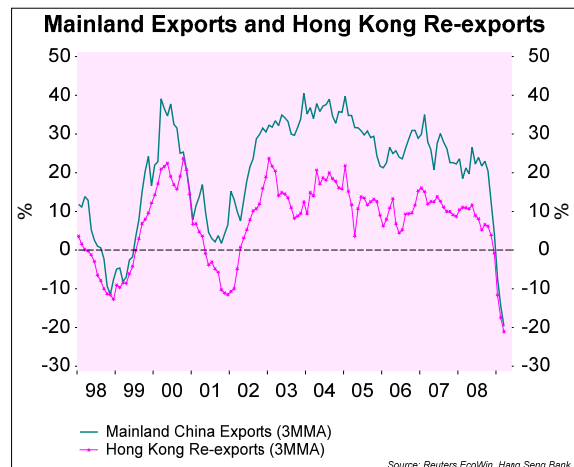
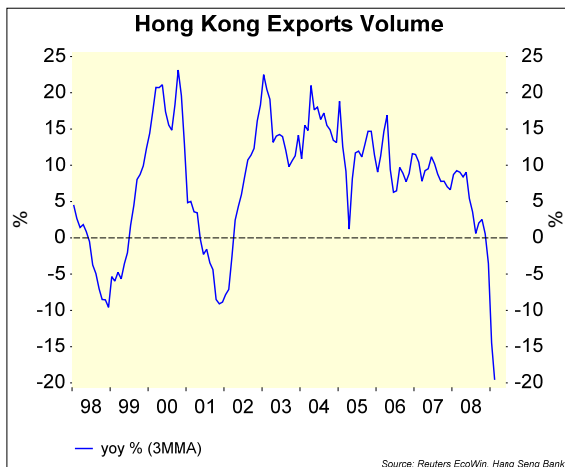
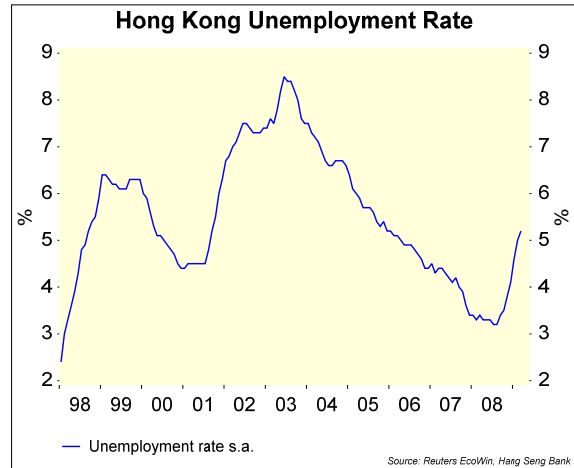
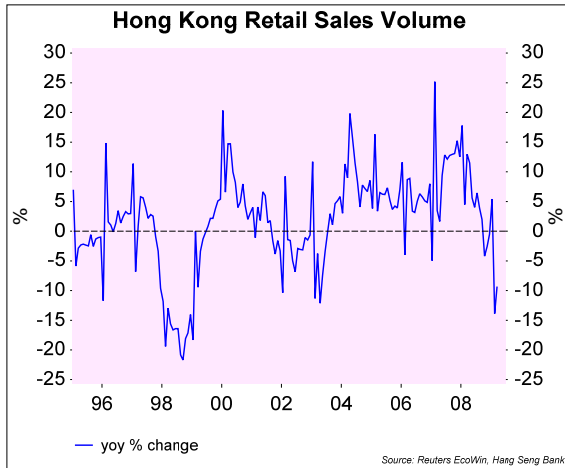
Source: Hong Kong's Census and Statistics Department

Going forward, inflation is going to ease further on depressing demand amid economic recession. The government's new property rate concessions would also suppress the headline inflation.

Inflation is thus likely to stay low for most of this year. Headline inflation may even slip into negative regions for some months, but not for a prolonged period. At this stage, we still expect consumer inflation to remain positive, averaging about 1.0% for 2009.

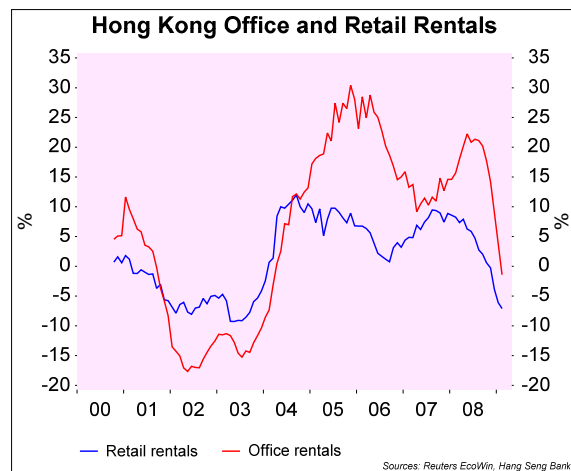
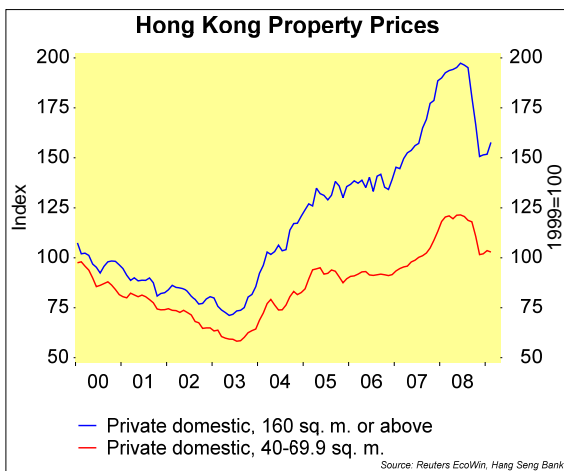
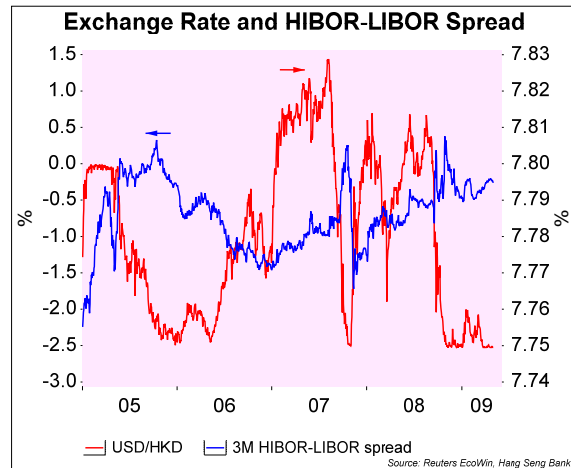
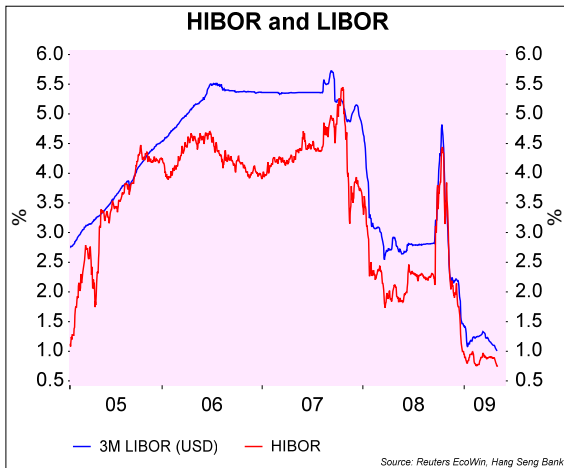
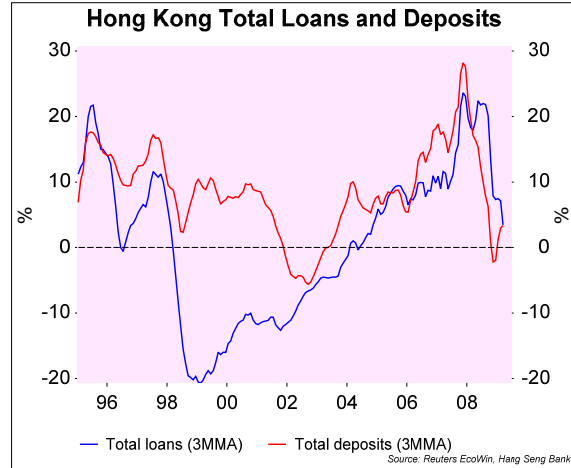
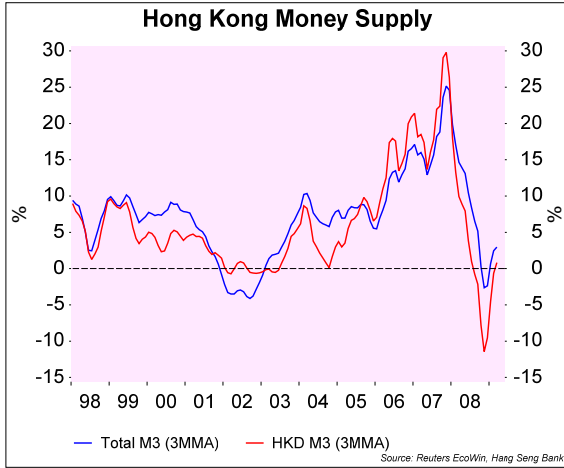
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## Hong Kong Economic Monitor Statistics

May 2009

|              | GDP (real)  | Real GDP per capita | Retail sales (real) | Total Deposits |             | Total Loans  |              | Money supply (Total M3) | Consumer prices | Unemployment rate (s.a.) |
|--------------|-------------|---------------------|---------------------|----------------|-------------|--------------|--------------|-------------------------|-----------------|--------------------------|
|              | yoy(%)      | yoy(%)              | yoy(%)              | HKD bn         | yoy(%)      | HKD bn       | yoy(%)       | yoy(%)                  | yoy(%)          | %                        |
| 2002         | 1.8         | 1.4                 | -2.6                | 3,318          | -2.6        | 2,076        | -5.0         | -0.9                    | -3.0            | 7.3                      |
| 2003         | 3.0         | 3.2                 | -0.6                | 3,567          | 7.5         | 2,035        | -2.0         | 8.3                     | -2.6            | 7.9                      |
| 2004         | 8.5         | 7.6                 | 9.1                 | 3,866          | 8.4         | 2,156        | 5.9          | 8.6                     | -0.4            | 6.8                      |
| 2005         | 7.1         | 6.6                 | 6.1                 | 4,068          | 5.2         | 2,312        | 7.3          | 5.2                     | 1.0             | 5.6                      |
| 2006         | 7.0         | 6.3                 | 5.8                 | 4,757          | 17.0        | 2,468        | 6.7          | 15.5                    | 2.0             | 4.8                      |
| 2007         | 6.4         | 5.3                 | 10.1                | 5,869          | 23.4        | 2,962        | 20.0         | 20.6                    | 2.0             | 4.0                      |
| 2008         | 2.5         | 1.7                 | 5.0                 | 6,060          | 3.2         | 3,284        | 10.9         | 2.6                     | 4.3             | 3.6                      |
| <b>2009F</b> | <b>-3.0</b> | <b>NA</b>           | <b>-8.0</b>         | <b>5,878</b>   | <b>-3.0</b> | <b>2,857</b> | <b>-13.0</b> | <b>1.5</b>              | <b>1.0</b>      | <b>6.3</b>               |
| Q3 2007      | 6.3         | NA                  | 12.6                | 5,694          | 25.1        | 3,042        | 21.8         | 22.3                    | 1.6             | 4.1                      |
| Q4           | 6.6         | NA                  | 13.5                | 5,869          | 23.4        | 2,962        | 20.0         | 20.6                    | 3.5             | 3.6                      |
| Q1 2008      | 7.3         | NA                  | 11.6                | 5,762          | 15.9        | 3,170        | 18.7         | 13.5                    | 4.6             | 3.4                      |
| Q2           | 4.2         | NA                  | 7.0                 | 5,706          | 7.1         | 3,349        | 17.1         | 5.7                     | 5.7             | 3.3                      |
| Q3           | 1.7         | NA                  | 4.1                 | 5,847          | 2.7         | 3,425        | 12.6         | 1.9                     | 4.6             | 3.4                      |
| Q4           | -2.5        | NA                  | -2.5                | 6,060          | 3.2         | 3,284        | 10.9         | 2.6                     | 2.3             | 4.1                      |
| Q1 2009      | NA          | NA                  | -5.5                | 6,022          | 4.5         | 3,166        | -0.1         | 2.6                     | 2.7             | 5.2                      |
| Nov 2008     | NA          | NA                  | -2.7                | 5,904          | -3.2        | 3,353        | 4.9          | -3.5                    | 3.1             | 3.8                      |
| Dec          | NA          | NA                  | -0.5                | 6,060          | 3.2         | 3,284        | 10.9         | 2.6                     | 2.1             | 4.1                      |
| Jan 2009     | NA          | NA                  | 5.4                 | 5,989          | 3.7         | 3,266        | 6.8          | 3.2                     | 3.1             | 4.6                      |
| Feb          | NA          | NA                  | -13.9               | 5,926          | 1.9         | 3,221        | 3.8          | 1.5                     | 0.8             | 5.0                      |
| Mar          | NA          | NA                  | -9.3                | 6,022          | 4.5         | 3,166        | -0.1         | 4.2                     | 1.2             | 5.2                      |
| YTD          | NA          | NA                  | -5.5                | 6,022          | 4.5         | 3,166        | -0.1         | 4.2                     | 2.7             | 5.2                      |

|              | Foreign Trade |             |              |             |               | Property Price Index | Office Rental Index | Tourist Arrivals |             | HKD per USD (end of period) |
|--------------|---------------|-------------|--------------|-------------|---------------|----------------------|---------------------|------------------|-------------|-----------------------------|
|              | Exports       |             | Imports      |             | Trade balance |                      |                     | '000             | yoy(%)      |                             |
|              | HK\$bn        | yoy(%)      | HK\$bn       | yoy(%)      |               |                      |                     |                  |             |                             |
| 2002         | 1,561         | 5.4         | 1,619        | 3.3         | -58.9         | -11.1                | -15.4               | 16,566           | 20.7        | 7.798                       |
| 2003         | 1,742         | 11.7        | 1,806        | 11.5        | -63.3         | -12.0                | -12.7               | 15,537           | -6.2        | 7.763                       |
| 2004         | 2,019         | 15.9        | 2,111        | 16.9        | -92.0         | 26.7                 | 4.6                 | 21,811           | 40.4        | 7.774                       |
| 2005         | 2,250         | 11.4        | 2,330        | 10.3        | -79.3         | 18.0                 | 23.5                | 23,359           | 7.1         | 7.753                       |
| 2006         | 2,461         | 9.4         | 2,600        | 11.6        | -138.8        | 0.7                  | 21.2                | 25,251           | 8.1         | 7.775                       |
| 2007         | 2,688         | 9.2         | 2,868        | 10.3        | -180.5        | 11.6                 | 12.1                | 28,169           | 11.6        | 7.801                       |
| 2008         | 2,824         | 5.1         | 3,025        | 5.5         | -201.1        | 16.4                 | 17.9                | 29,500           | 4.7         | 7.750                       |
| <b>2009F</b> | <b>2,612</b>  | <b>-7.5</b> | <b>2,774</b> | <b>-8.3</b> | <b>-162.0</b> | <b>-18.0</b>         | <b>-18.0</b>        | <b>28,763</b>    | <b>-2.5</b> | <b>7.800</b>                |
| Q3 2007      | 720           | 8.2         | 757          | 9.4         | -36.6         | 12.2                 | 10.9                | 7,334            | 15.1        | 7.767                       |
| Q4           | 729           | 8.2         | 781          | 10.5        | -52.0         | 21.4                 | 14.0                | 7,806            | 16.9        | 7.801                       |
| Q1 2008      | 698           | 10.5        | 647          | 11.6        | -51.4         | 29.5                 | 16.1                | 7,276            | 10.0        | 7.781                       |
| Q2           | 706           | 7.9         | 773          | 9.2         | -67.6         | 25.6                 | 21.1                | 6,910            | 7.7         | 7.818                       |
| Q3           | 809           | 5.5         | 760          | 6.8         | -48.4         | 18.5                 | 20.8                | 7,583            | 3.4         | 7.763                       |
| Q4           | 714           | -2.1        | 748          | -4.2        | -34.2         | -4.6                 | 13.6                | 7,722            | -1.1        | 7.750                       |
| Q1 2009      | 505           | -21.9       | 539          | -22.8       | -34.3         | -14.0                | -2.1                | 7,404            | 1.8         | 7.751                       |
| Nov 2008     | 231           | -5.3        | 239          | -7.9        | -8.2          | -7.4                 | 14.4                | 2,422            | -1.1        | 7.750                       |
| Dec          | 206           | -11.4       | 218          | -16.2       | -11.8         | -11.1                | 9.0                 | 2,768            | -0.8        | 7.750                       |
| Jan 2009     | 188           | -21.8       | 181          | -27.1       | 7.2           | -13.1                | 3.3                 | 2,796            | 11.0        | 7.756                       |
| Feb          | 142           | -23.0       | 165          | -17.5       | -23.2         | -14.4                | -2.3                | 2,162            | -8.1        | 7.756                       |
| Mar          | 175           | -21.1       | 194          | -22.7       | -18.2         | -14.5                | -7.2                | 2,445            | 1.7         | 7.751                       |
| YTD          | 505           | -21.9       | 539          | -22.8       | -34.3         | -14.0                | -2.1                | 7,431            | 1.8         | 7.751                       |

Note: (F) Forecast

Source: CEIC, Hang Seng Bank







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