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Assessment of the Strengths and Prospects of Hong Kong's Economic Growth

Dr. E Zhihuan, Chief Economist, Bank of China (Hong Kong)

The global economy recovers strongly in 2021, with GDP growth in all major economies exceeding their potential economic growth levels. Looking ahead to 2022, the global economy will not be able to escape the uncertainties brought about by the coronavirus pandemic, with economic growth and inflation likely to diverge between advanced economies and emerging markets due to differences in the progress and effectiveness of vaccination. As a typical small and open economy, Hong Kong has generally benefited from economic growth in Mainland China and easing policies in the United States. In the first three quarters of 2021, Hong Kong's GDP grew by 7% year-on-year. Despite a slight slowdown in the third quarter, the Hong Kong economy is expected to grow by more than 6% for the whole 2021, recovering from six consecutive quarters of contraction in 2019 and 2020 and returning to levels before the pandemic.

1. Hong Kong recovers in tandem with other major economies

As a typical small and open economy, Hong Kong's economy has always reflected the shifting dynamics of the global economic recovery and has been directly influenced by the growth dynamics and macro policy adjustments of Mainland China and the US. Globally, the underlying logic for economic growth in 2021 is the low base and stimulus effects of accommodative fiscal and monetary policies in coping with the economic downturn in the first half of 2020.

For the first three quarters of 2021, the US economy grew by an annual rate of 5.7%, outpacing its pre-pandemic growth by about 1.4%, reflecting recovery driven by economic reopening and easing policies. The pace of US GDP growth slowed in the third quarter, with the annual pace falling to 4.9% and the annualized quarter-on-quarter pace moderating to 2%. The supply chain was bottlenecked and unable to meet the demand from the economic reopening due to the recurrent waves of pandemic outbreak and severely disrupted supply chains in some sectors, with auto production and sales, inventory changes and residential investment reacting particularly strongly and to continue into the fourth quarter. Taking into account the effects of fiscal stimulus and ultra-loose monetary policy, the US economy is expected to increase 5.5% this year, below the International Monetary Fund's forecast of 6%.

Some segments of the US economy are still growing, with the October's Manufacturing Index from the Institute for Supply Management (ISM) and the Housing Market Index from National Association of Home Builders (NAHB) falling from their year-to-date highs of 64.7 and 84 respectively, but still hovered at high levels of 60.8 and 80, indicating that there is no significant change of the momentum of the US economic recovery. The University of Michigan's Consumer Sentiment Index fell to 66.8 in November from a high of 88.3 in April this year, due to the elevated inflation and the recurring waves of pandemic outbreak.

The US labour market continues to improve. The number of non-farm payrolls increased by 531,000 in October, in line with market expectations, and the figures for August and September were both revised upward. The monthly average number of non-farm payrolls added in the past six months reached 666,000, and the unemployment rate fell further by 0.2 percentage points to 4.6% in October. Currently, comparing with their pre-pandemic levels, the unemployment rate is 1.1 percentage points higher, the number of existing non-farm payrolls is 4.2 million lower, and the labor force participation rate and employment-to-population ratio are 1.7 and 2.3 percentage points lower, respectively. The labor market indicators above have not yet returned to their pre-pandemic levels and are expected to continue to trend toward full employment in 2022.

The eurozone's economic growth in the first half of 2021 was relatively fast, and was affected less than expected by the repeated pandemic outbreaks. Recently, the IMF raised its forecast for the eurozone growth by 0.4 percentage points to 5% for 2021, while the forecast for 2022 remained unchanged at 4.3%, both significantly exceeding the average economic growth of the eurozone in recent years. In July 2021, the European Central Bank (ECB) reviewed its monetary policy framework, proposing six key points that would slightly increase the inflation target while placing greater emphasis on symmetry in response to the new environment of high inflation in the single currency zone and provided the policy basis for its continued ultra-loose monetary policy.

In the first three quarters of this year, the Chinese economy grew by an average rate of 9.8%, with a two-year average rate of 5.2%. Since the third quarter, China's merchandise exports, industrial production, fixed asset investment and retail sales have all slowed down due to the combined effects of the low base, tightened restrictions on social distances and economic activities following the outbreak of pandemic in some regions, double controls of energy consumption and restrictions on electricity consumption, as well as strengthened regulatory controls on several industries. It is expected that exports could continue to benefit from improving external environment in the fourth quarter, while industrial production and manufacturing investment will also grow. Some industries will face the adverse effects of rising raw material prices and double controls of energy consumption. Fixed asset investment will depend on fiscal, monetary, and real estate policy adjustments, consumption is also uncertain due to the pandemic and the recovery of the labour market. With the support of accommodative macro policy, low base and economic reopening, China's economy will grow about 8% in 2021.

Since 2021, Hong Kong's exports have performed well, benefiting from the reliance of major global economies on China's merchandise goods. External demand has maintained a relatively large contribution to economic growth in Hong Kong. At the same time, factors such as the contained local pandemic, the release of consumer vouchers and the low base of last year's economic growth have supported stronger consumption and boosted the performance of domestic demand.

Hong Kong's economy grew by an annual pace of 7% in the first three quarters of 2021, with signs of a slowdown in the third quarter. In terms of monthly data, Hong Kong's tourism industry remained frozen, service exports failed to improve, imports of goods grew higher than exports, and net exports contributed less to economic growth, partly due to a higher base in the third quarter of last year than in the first half, with a difference of 5.5 percentage points between the two.

2. Hong Kong's labour market improves significantly

Since March 2021, Hong Kong's labour market has improved markedly due to the economic recovery, improvement in the local pandemic containment and residents' adaptation to social distancing measures, with the unemployment rate falling rapidly. The unemployment rate in Hong Kong further declined to 4.3% in August-October, down 0.2 percentage points from July-September, and down 2.9 percentage points from a high of 7.2% in December 2020-February 2021.

The rapid improvement in the labour market is conducive to a stable economic recovery. Meanwhile, the Hong Kong Vaccination Programme has started from the end of February 2021, and so far about 70% of eligible people have been vaccinated. Coupled with effective anti-pandemic measures, the pandemic has been gradually under control and local economic activities have returned to normal level. Starting from August 2021, the government has issued different batches of consumption vouchers to further boost the performance of domestic consumption and drive the labour market improvement.

The unemployment rates in Hong Kong's retail, accommodation and food services, construction and manufacturing sectors have improved somewhat from their high levels at the beginning of the year, but the unemployment rates in August-October were still high at 6.9%, 6.4% and 6.1% respectively, indicating that the above sectors continue to be hit by stringent pandemic control measures, the continued suspension of tourism and the fact that international travel has not yet resumed. The unemployment rate of these sectors is 2.6 percentage points higher than the overall unemployment rate, indicating that the employment situation of some grassroots citizens continues to be grim.

The labour market performance reflects the dynamic evolution of shocks from the Covid-19 pandemic, with the overall unemployment rate in Hong Kong rising to 7.2% in December 2020-February 2021, a record high since the first quarter of 2004, and a sharp jump from the 2.8% in mid-2019.

Recently, Hong Kong's economic activities have gradually recovered and some of those who were unemployed earlier have re-entered the labor market. The labor force participation rate in July-September 2021 was 59.3%, 1.2 percentage points lower than the same period in 2019 before the pandemic, and this will drive the labour market toward full employment.

The Composite Consumer Price Index rose moderately by 1.7% in October. The continued economic recovery and rising import prices have increased short-term inflationary pressures, but the Hong Kong economy is operating below the level of production capacity to effectively control inflationary pressures, with underlying inflation rising by only 0.5% in the first ten months of the year.

3. Major global economies seek new growth paths in 2022

The global economy will unlikely be free from the uncertainties brought by the pandemic. The advanced economies and emerging markets may show a double divergence of economic growth and inflation due to the differences in the progress of pandemic control and vaccination.

1) The race between further virus variations and the penetration and effectiveness of vaccines will redefine the logic of global economic growth in 2022.

The global economy in 2022 is likely to show a double divergence in growth and inflation between advanced economies and emerging markets due to differences in the progress of pandemic control and vaccination. Currently, it appears that despite the high vaccination rates in advanced economies and the announcement by Merck and Pfizer to develop new oral drugs to reduce the risk of hospitalization or death from the coronavirus, herd immunity has not yet been established and the rate of severe illness and death is still much higher than that of the common flu. The impact of the pandemic on the economy and service industry still needs to be observed.

2) Disruptions in the supply chain could lead to a longer-than-expected impact of price increases, exacerbating inflationary pressures and prompting advanced economies to reassess their monetary policies stance

Inflationary pressures have risen in the US since 2021, with the Federal Reserve's preferred measure of inflation, the Personal Consumption Expenditure (PCE) index and its core index rising 4.4% and 3.6% year-on-year in

September to new highs since January 1991 and May 1991, respectively. The Consumer Price Index (CPI) and its core index rose 6.2% and 4.6% year-on-year in October to new highs since November 1990 and August 1991, respectively. Food, used car, energy and housing prices rose by 5.3%, 26.4%, 30.0% and 3.5%, respectively, amid the supply and transportation disruptions and lower labour force participation rate.

Recently, the Federal Reserve has changed its judgment that inflation is transitory. Previously, inflation pressures were concentrated in durable goods, energy, hotel and airfares, but were associated with a low base, work-from-home arrangements, and supply chain disruptions. Inflation pressures of some of the earlier items with high price increases have moderated. Currently, short-term yields on US bonds have responded to the expected rate hikes, while long-term yields have risen less and the gap between 10-year and two-year yields on US government bonds has narrowed. However, the normalization of US monetary policy is a long road, and the accommodative monetary policy environment will not significantly change in the short term.

3) Easing policies in major economies have resulted in high debt and large fiscal deficits that are not sustainable. Shifts in monetary policy stance has been initiated, but the pace of it will continue to be disrupted by the development of the pandemic

At the Federal Reserve's November meeting, the Fed maintained the federal funds rate at 0% - 0.25% and announced that it would reduce its bond purchases to zero by mid-June 2022 by cutting USD10 billion of US Treasuries and USD5 billion of mortgage-backed securities each month. From November 2021 to mid-June 2022, the bond purchases will total USD420 billion, down from USD840 billion if without the tapering. The Fed's balance sheet will continue to expand, but at a slower pace, and is expected to grow to just over USD9 trillion by mid-2022, an increase of about 120% from the pre-pandemic level of USD4.15 trillion. A cycle of federal funds rate hikes will follow the completion of the Taper.

Inflation in Europe's major economies is under upward pressure, with the inflation rate in the eurozone rising to 4.1% year-on-year in October 2021, a significant acceleration from 3.4% in September and a new high since July 2008. In March 2022, the ECB will complete its pandemic emergency purchase programme (PEPP) as planned but may extend its asset purchase program of EUR20 billion per month and make new arrangements for the interface between the two. In 2022, inflation in the Eurozone is likely to remain elevated, limiting to a certain extent the room for further monetary easing by the ECB. Therefore, the ECB is expected to maintain its current monetary policy in the medium term and, depending on the future performance of inflation, to decide on the timing and extent of interest rate hikes. The global monetary environment will remain accommodative. Overall, the shift in monetary policy in Europe will lag behind other major economies and support a continued accommodative global monetary environment.

4. China's economic growth continues to lead

In 2022, China's economy will continue to grow, with slight adjustments of double control on energy consumption, industry regulation and growth stabilization policies, and a largely contained pandemic will support recovery in economic and social activities. On the one hand, its exports will continue to benefit from the global economic recovery, and the large-scale economic stimulus measures in Europe and the US and the disruption of production in some regions due to the pandemic will further boost the demand for Chinese goods, which will be conducive to the improvement of industrial production and investment in manufacturing. However, some industries are constrained by rising raw material prices and double control of energy consumption. Fixed asset investment will depend on fiscal, monetary, and real estate policy adjustments, while consumption will depend on the outbreak of the pandemic in individual regions and the prospects for labour market recovery, as well as the extent to which the overall income level of residents will rise.

There is still relatively large policy room to stabilize growth in China. Monetary policy has put more emphasis on flexibility, precision, reasonableness and appropriateness, with self-interest as the main focus and stability at the forefront, performing cross-cycle adjustment, coordinating the policy convergence between this year and next, maintaining a reasonable abundance of liquidity and enhancing the stability of total credit growth. In October 2021, the growth rate of social financing fell to 10% from a high of 13.3% year-on-year in February, and the growth rate of money supply (M2) slowed to 8.7% from 10.1%. The growth rate of money supply and social financing basically matched the growth rate of the nominal GDP, helping small and medium-sized enterprises and industries in difficulties to continue to recover, and enhancing macro policy autonomy to maintain the RMB exchange rate at a reasonable balance level. The July cut of RRR is a precautionary measure to prevent a further slowdown in economic growth, to support SMEs against rising commodity prices and to offset the impact of weak fiscal policy growth, rather than the start of a new round of easing measures.

Recently, China launched a carbon emission reduction support tool to provide funds to banks that provide related loans, offering targeted easing support to offset downward pressure in the short term, while helping to achieve the goal of carbon emission reduction in the long term. At the same time, it will further leverage the leading role of measures such as relending, re-discounting and direct monetary policy tools for the real economy to support increased lending to small and micro enterprises and individual entrepreneurs. It will continue to maintain an orderly slowdown in credit growth and provide differentiated credit support to individual industries and enterprises, complemented by prudential supervision measures to address a range of financial stability issues related to housing, local government debt and shadow banking. A variety of monetary policy tools, such as medium-term lending facilities (MLF) and open market operations, will be used to maintain a reasonable level of liquidity, and the probability of a slight adjustment of the reserve requirement ratio (RRR) and a slight policy interest rate cut for the rest of the year is expected to be low.

The focus of fiscal policy in 2021 is restoring the economy, stabilizing employment, and increasing revenue. The fiscal deficit rate of about 3.2% and the size of new government special bonds similar to that of 2020 are more supportive than expected, and there is ample fiscal space in the second half of the year. In the first nine months of 2021, fiscal expenditure grew by only 2.3% year-on-year, fiscal revenue grew by 16.3%, while the issuance of local government special bonds accounted for about 84% of its annual quota, indicating that there is still room for fiscal policy support. In 2022, fiscal policy will continue to promote stable credit growth, which will be conducive to promoting investment growth in infrastructure and ensuring that the economy can transition to a normalized level in a stable manner.

The new era of China's economy is characterized by slower growth, tighter regulation, and deleveraging. The responsibility for economic regulation and risk management will fall on macro policies, while industry and regulatory policies will serve to achieve financial stability, structural adjustment, and long-term economic and social development needs. Regulation will also be adapted to the needs of new economic sectors and will balance profitability with social responsibility to achieve common prosperity, national interest, and security. In the future, fiscal and monetary policies will continue to play a major role in managing macroeconomic performance and controlling risks.

In the face of the unprecedented changes in the past hundred years, the 14th Five-Year Plan of China has creatively proposed the concept of promoting dual circulation, in which domestic circulation is a mainstay, and domestic and international circulation boost each other. The domestic circulation will strengthen internal reform, promote market-oriented reform of production factors, make up for the shortcomings in the production field, forge a long version, and gradually narrow the gap between the rich and the poor in the distribution field to achieve common prosperity. The international circulation will focus on opening-up, accelerating the opening of the financial market from the perspective of trade layout and production liberalization, relaxing market access, and continuing to enhance the scope of RMB outreach and internationalization.

5. Continuing growth is expected of Hong Kong's economy in 2022

In the long run, Hong Kong's role as a participant in the domestic circulation and a facilitator of the international circulation in the country's dual circulation pattern will bring constant impetus to economic development. The 14th Five-Year Plan clearly states that Hong Kong should consolidate its traditional strengths and enhance its status as an international financial centre, international shipping center, international trade center, trade and legal dispute resolution services center. At the same time, Hong Kong should create new strengths by building a center for innovation and technology, developing a center for cultural and artistic exchanges, a trade center for intellectual property rights, and consolidating its status as an international aviation hub. This provides a new entry point for Hong Kong's integration into national development. This year's Policy Address highlights the need to make good use of national support for the development of Hong Kong's four traditional centers, and to master the positioning of the four emerging centers, with new measures and breakthroughs to set the stage for Hong Kong's development.

In the short to medium term, Hong Kong's economic growth will still depend on changes in the surrounding environment.

The IMF expects the global economy to grow by 4.9% in 2022. The implied premise is that advanced economies are constrained by supply disruptions, emerging and developing economies are hit by the pandemic, and the spread of virus variants increases uncertainty about the development of the pandemic, making it difficult for the global economy and cross-border flows to fully return to normal and achieve a stable recovery in the near term, basically continuing the actual trajectory of 2021.

In 2022, from a global perspective, the impact of the coronavirus will continue, vaccination rates will increase and there will be breakthroughs in drug development. The impact of the repeated pandemic outbreaks on the global economic recovery remains to be seen, and the normalization of loose monetary policy will not significantly change the low interest rate and abundant liquidity environment, bringing support to the global and Hong Kong economies.

If inflation in advanced economies remains high in the future, the Federal Reserve may change its view that inflation is transitory, and then adjust the timing and pace of its bond purchases and interest rate hikes, which may trigger a new round of volatility in the financial markets, and we should remain highly alert to the external risks that may arise.

During the period when the pandemic is under good control and with effective risk control, Hong Kong can gradually expand the arrangement for Mainland residents to come to Hong Kong with exemption on quarantine, promote the recovery of tourism, further improve service exports, and jointly enhance the contribution of external demand to Hong Kong's economic growth. With the advancement of universal vaccination, social distancing measures such as the Gathering Restriction Order can be adjusted according to the changes of the pandemic to reduce the impact of the siege and mandatory quarantine on the consumption and services sectors, to contain its shocks on the real economy.

At present, the Hong Kong government is working hard to obtain traveler clearance with the Mainland to enhance the impetus of cross-border tourism and retail trade to the overall economic recovery. The government will continue to issue consumer vouchers in different batches in the fourth quarter, which will continue to boost consumption. It is expected that the Hong Kong economy and the employment market will further recover in this and next year, and the unemployment rate may decline further in 2022.

The Hong Kong government expects Hong Kong's economic growth to reach 6.4% in 2021, with the economy returning to 2019 levels. In 2022, the economy will be able to maintain a relatively stable growth rate and build up new momentum for long-term economic development.

主要經濟指標 (Key Economic Indicators)

	2019	2020	2021/Q2	2021/Q3
一. 本地生產總值 GDP				
總量(億元) GDP($100 Million)	27,997	26,277	6,757	7,205
升幅(%) Change(%)	-1.2	-6.1	7.6	5.4
二. 對外貿易 External Trade			**2021/10**	**2021/1-10**
外貿總值(億元) Total trade($100 Million)				
總出口 Total exports	40,961	39,275	4,183	39,988
進　口 Total imports	45,714	42,698	4,487	43,005
貿易差額 Trade balance	-4,753	-3,422	-305	-3,017
年增長率(%) YOY Growth(%)				
總出口 Total exports	-5.6	-1.5	21.4	26.7
進　口 Imports	-8.1	-3.3	17.7	25.5
三. 消費物價 Consumer Price				
綜合消費物價升幅(%) Change in Composite CPI(%)	2.9	0.3	1.7	1.5
四. 樓宇買賣 Sale & Purchase of Building Units			**2021/10**	**2021/1-10**
合約宗數(宗) No. of agreements	74,804	73,322	6,250	81,818
年升幅(%) Change(%)	-5.5	-2.0	1.0	39.9
五. 勞動就業 Employment			**2021/7-2021/9**	**2021/8-2021/10**
失業人數(萬人) Unemployed(ten thousands)	139	259.1	18.1	17.2
失業率(%) Unemployment rate(%)	2.9	5.5	4.5	4.3
就業不足率(%) Underemployment rate(%)	1.1	3.1	2.1	1.9
六. 零售市場 Retail Market			**2021/10**	**2021/1-10**
零售額升幅(%) Change in value of total sales(%)	-11.1	-24.3	12.0	8.5
零售量升幅(%) Change in volume of total sales(%)	-12.3	-25.5	9.4	7.1
七. 訪港遊客 Visitors				
總人數(萬人次) arrivals (ten thousands)	5,590	356.9	0.9	7.2
年升幅(%) Change(%)	-14.2	-93.6	19.6	-98.0
八. 金融市場 Financial Market			**2021/9**	**2021/10**
港幣匯價(US$100=HK$) H.K. Dollar Exchange Rate (US$100 = HK$)	779.3	775.2	778.8	778.1
貨幣供應量升幅(%) change in Money Supply(%)				
M1	2.6	30.1	0.1	-15.6
M2	2.8	5.8	1.4	-4.3
M3	2.7	5.8	1.4	-4.2
存款升幅(%) Change in deposits(%)				
總存款 Total deposits	2.9	5.4	1.6	-4.4
港元存款 In HK$	2.5	6.2	-2.2	-11
外幣存款 In foreign currency	3.2	4.6	5.6	3.2
放款升幅(%) in loans & advances(%)				
總放款 Total loans & advances	6.7	1.2	-0.1	-4.8
當地放款 use in HK	7.1	1.7	-0.1	-6.9
海外放款 use outside HK	5.8	0.1	0.1	0.8
貿易有關放款 Trade financing	-0.7	-6.2	25.3	18.8
最優惠貸款利率(%) Best lending rate (%)	5.0000	5.0000	5.0000	5.0000
恒生指數 Hang Seng index	28,189	27,231	24,576	25,377