CHINA ECONOMICS UPDATE

Hong Kong's recovery to benefit from fiscal support

- **With Hong Kong's economy on the mend, the budget unveiled today curtailed some of last year's emergency spending. But it still signals a supportive fiscal stance, particularly in areas hardest hit by COVID. Together with the reopening of Hong Kong's borders and end of virus-related restrictions, we continue to expect robust growth this year.**
- Financial Secretary Paul Chan announced today that the budget deficit for FY 2023/24 (starting in April) is expected to equal HKD54bn, or 2.0% of 2022 GDP. This is a big step down from the HKD 140bn deficit (5.1% of GDP) in the current fiscal year. That is mainly due to a 6% pull-back in spending. **But with spending almost 25% higher than in FY2019, the fiscal taps will still be running.**
- Among the more eye-catching measures is a further disbursement of consumption vouchers worth HKD5,000 to each adult, at a total cost of 1.1% of 2022 GDP. HKD3,000 will be handed out in April, and the remainder in the middle of the year. What's more, concessions will be offered on income and property taxes, each household will receive a one-off HKD1000 electricity subsidy, and low-income households will receive an additional one-off cash transfer equal to half a month of welfare benefits. Companies will also benefit: concessions will be offered on rates for non-domestic properties and rents for six months, and the first HKD6,000 of profit tax will be waived.
- To prop up the tourism and transportation industry, the government will guarantee business loans in these sectors up to HKD2.7bn. This support is especially timely given the rapid return of foreign visitors. Arrivals have rebounded strongly since border restrictions were relaxed at the start of the year, and currently stand at around 20% of 2018 levels. (See Chart 1.) **Together with previously announced promotional initiatives, today's measures should ensure a recovery in the transport, retail and hospitality sectors to pre-pandemic levels, if not quite to the pre-protest highs.**
- **The property market remains the major risk.** Today's budget stated that cooling measures on the property market will be maintained despite home prices tumbling 16% since mid-2021. Elevated interest rates will leave home prices vulnerable to further falls. And with real estate accounting for almost 80% of household wealth in the city, price declines could weigh heavily on consumer confidence and private consumption. The bigger picture, however, is that home prices are still elevated and affordability remains stretched. To alleviate the burden on first-time homebuyers, the tax rate for properties under HKD9m will be reduced.
- **The government has room to do more too and probably would if the drag from the property sector became significant**. The government has shown that it is willing to step in when the economy is faced with a negative shock in the past. (See Chart 2.) The fiscal reserves that are being used to finance the deficit remain substantial – they were worth 28% of GDP at the end of 2022.
- Overall, we are comfortable with our above-consensus forecast for 5.5% growth this year, up from a 3.5% contraction in 2022. The consensus estimate is 3.3% while the government has projected 3.5%-5.5%.

Chart 1: Arrivals into Hong Kong (% of 2018)

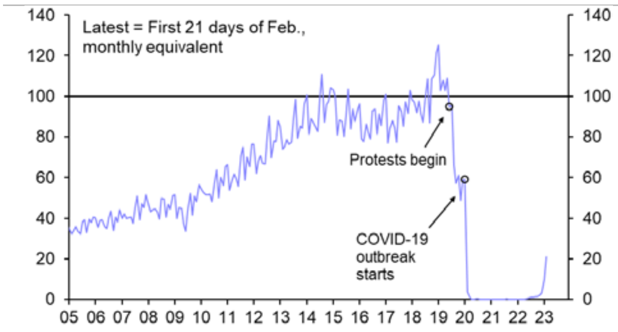
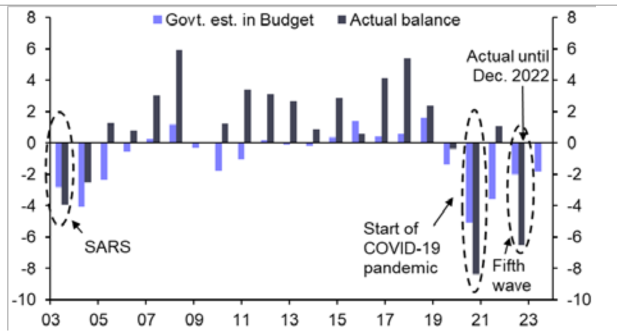


Chart 2: Hong Kong Budget Balance (% of GDP)



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