



GDP Observatory

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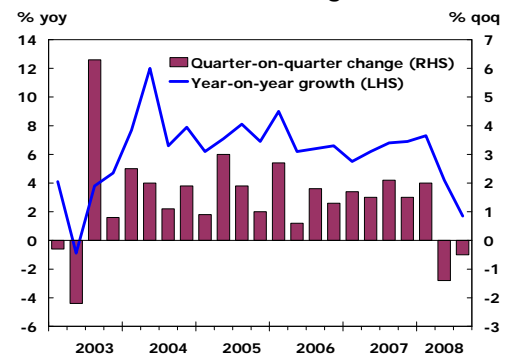
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Hong Kong falls into recession amidst the worst post-war global financial crisis

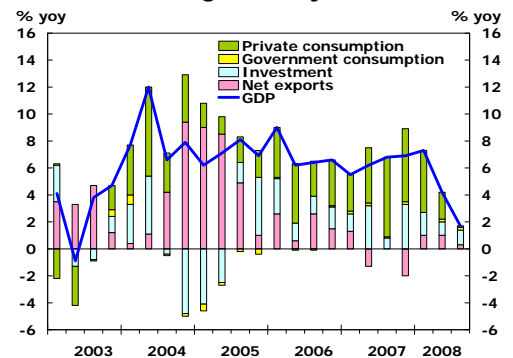
- Hong Kong's real GDP grew by 1.7% yoy in Q3, following a strong 4.2% growth in Q2 (Chart 1). The Q3 figure is much lower than the market consensus of 2.6%, suggesting the slowdown has accelerated.
- On a seasonally adjusted qoq basis, real GDP contracted by 0.5%, the second consecutive quarterly contraction. Thus, the Hong Kong's economy has fallen into a recession.
- With respect to real GDP by expenditure, private consumption expenditure (PCE) slowed to 0.2% yoy in Q3, compared with 3.2% yoy in Q2. The negative wealth effect due to a sharp drop in the stock market and investment losses in financial derivatives products have contributed to the sharp fall in PCE growth. Meanwhile, a large fall in labour market sentiments since the collapse of the Lehman Brothers has also contributed to the precautionary savings motives, thus leading to the sharp deterioration in PCE. Government consumption remains supportive at 2.3% in Q3 compared with 3.0% in Q2 due to increased spending on subsidies and other relief measures in the last quarter. Investment growth slowed to 3.0% yoy from 3.5% in Q2 on negative growth outlook in the coming quarters.
- While both exports of goods and services slowed considerably to 1.4% and 5.3%, respectively, on slowing re-exports passing through Hong Kong, imports of both goods and services fell even more sharply to 2.2% and 1.8%. As a result, net exports of goods and services still contributed positively to real GDP growth (Chart 2).
- Relative to Singapore's growth of -0.5% yoy in Q3, Hong Kong's economic slowdown was less severe, benefiting from the still robust, though much slowed, export growth on Mainland China.
- The business tendency survey in Q4 suggests that Hong Kong's economic conditions will continue to deteriorate in the coming quarters on sharply deteriorating outlook of the global economy (Chart 3).

Chart 1: Real GDP growth



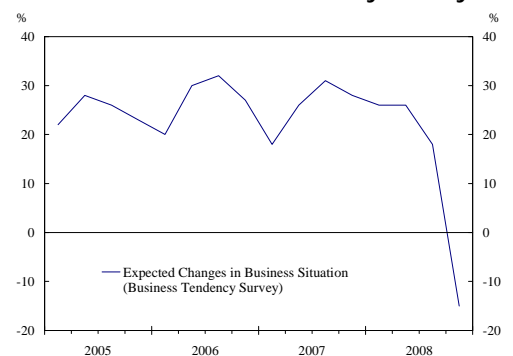
Source: Census and Statistics Department, HKSAR.

Chart 2: GDP growth by contribution



Source: Census and Statistics Department, HKSAR.

Chart 3: Business Tendency Survey



Sources: Census and Statistics Department, HKSAR & CEIC.

- Looking forward, we expect growth in Hong Kong to continue to slide further, led by a simultaneous, severe, and possibly protracted recession in the G-3 economies.
- We forecast the Hong Kong economy to grow by 3.0% in 2008 and -1% in Q4 2008. The economic growth in 2009 is forecasted to grow at 1.5%, much lower than its economic potential at 4-5%.
- Given the sharply deteriorating demand, inflationary pressure is diminishing at a fast pace. We forecast the underlying CPI inflation to stay at an averaged 5.1% in 2008 and reach an averaged 1.0% in 2009. The risk of a return of deflation has increased.

Chart 4: GDP and Inflation Forecast

