Economic Research

October 2022

Market Monitor – Hong Kong

First Prime Rate Hike in 4 Years

Hong Kong banks raised prime rates following Fed's rate hike

After the US Federal Reserve (Fed) raised interest rates by 300 bps since March 2022, bringing its policy rate to the highest level since 2008, the surge in Hong Kong's interbank rates eventually drove commercial banks to announce the city's first prime rate hike in over 4 years with an increase of 12.5 bps. While the rate hike was well anticipated, the scale is relatively timid given the ample base of savings and demand deposits. The share of savings and demand deposits in licensed banks is still high at 64.4% as of July 2022, significantly above the 59.9% recorded in March 2005 and 60.5% in September 2018, when Hong Kong's last two rate hike cycles began. Looking forward, upside pressures on the HKD prime rate are expected due to the Fed's policy tightening, rising HIBORs, some migration of saving and demand deposits, etc., though the upside pressure should remain moderate. The HKD prime rate may only rise to 5.5% by the end of 2022, implying a further rise of 37.5 bps in Q4.

Mandatory hotel quarantine ended for overseas arrivals

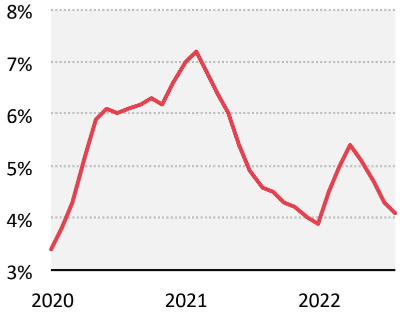
Hong Kong has ended its mandatory hotel quarantine requirements for overseas arrivals starting from 26th September, marking a further step in easing the stringent entry restrictions since the start of the pandemic, although arrivals still have to do 3 days of medical surveillance. Looking ahead, the pandemic measures appear to point towards a further re-opening ahead as the threat of pandemic recedes and in response to increasing expectation from the businesses community.

Hong Kong banks raise HKD prime rate by 12.5 bps, the first hike since September 2018.

End of mandatory hotel quarantine for overseas arrivals signals a further easing of entry restrictions ahead.

Domestic activity continues to recover, but external trade outlook is subject to further downside pressure.

Hong Kong Unemployment Rate



Source: Hong Kong Census and Statistics Department, data as of 30/9/2022

Domestic activity to pick up further but external trade stays sluggish

The jobs market has continued to see solid recovery as the seasonally-adjusted unemployment rate fell again to 4.1% in June-August, down from the earlier peak of 5.4%. Pandemic-sensitive sectors (namely retail, accommodation, and food services) continue to see significant improvements. Retail sales declined by 0.1% year on year (YoY) in August, while sales volume dropped 2.9%, despite the support from the new round of consumption vouchers and a rather quick recovery in the jobs market. While a full recovery of the retail sector still hinges on how quickly inbound tourism can return to normal (especially mainland visitors), a stable pandemic situation and employment market should give some boost to consumer confidence and domestic economic activity.

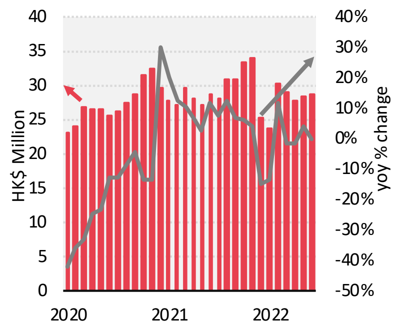
Contrary to the stabilising domestic environment, Hong Kong's export sector is beset by prevailing headwinds amid mounting global risks, including rapid monetary tightening by major central banks, supply chain disruption, elevated inflationary pressure, and a potential shift of consumer demand from goods to services following the global economic reopening. Merchandise exports contracted by 14.3% YoY in August, marking the fifth decline in the past 6 months amid a worsening external environment and disruption to cross-border land transport, while merchandise imports saw another significant YoY fall of 16.3% in August. The monthly trade deficit shrank from HK$68.5 billion in June to HK$27.6 billion in July and HK$13.3 billion in August, which superficially improved the economic picture.

Property market sentiment suppressed by rising interest rates

1-month HIBORs had climbed to 2.62% as of end-September, up 247 bps from the start of the year, while 3-month HIBORs had risen to 3.33%, up 308 bps from the start of the year. As the Federal Reserve is unlikely reverse its tight policy stance until 2024, we may see 1-month HIBORs exceeding 3.8% and 3-month HIBORs exceeding 4.2% by end-2022.

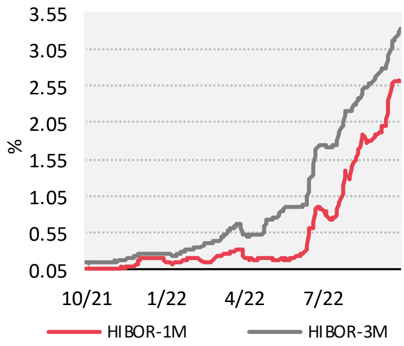
Property market sentiment has undoubtedly been dampened by the rising mortgage rates and uncertain global economic outlook. According to the latest data from the Rating and Valuation Department, Hong Kong residential property prices dropped 2.3% month on month (MoM) in August or 6.5% year-to-date (YTD), while rents saw another MoM rebound of 0.7% in August, with some housing demand possibly being diverted into the rental market. Residential prices may see a high single-digit correction this year, and the drop in rents may narrow further to 2% or lower. Although the property market is still subject to some downside pressure, a steady housing policy and the supply environment may mitigate the risk of a sharp property market correction in the near term. A recovering economy, a loosened stress test for mortgage loans, and a more balanced population flow after the easing of entry restrictions may help boost demand in the residential property market, assuming the rise in the prime rate remains manageable in the medium-to-long term.

Hong Kong Retail Sales



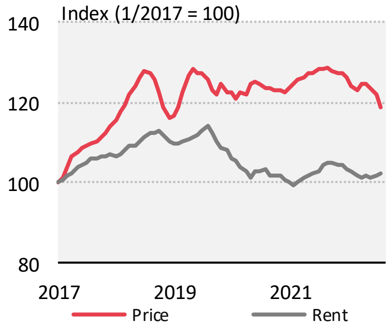
Source: Hong Kong Census and Statistics Department, data as of 30/9/2022

Hong Kong Interbank Rates



Source: Bloomberg, data as of 30/9/2022

Housing Price and Rent Indices

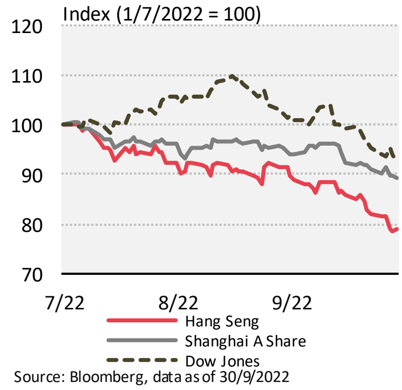


Source: Rating and Valuation Department, data as of 30/9/2022

Hong Kong equities fall to lowest point over a decade

Concerns over the Fed's rapid tightening actions and global economic outlook continue to dent market sentiment, causing the Hang Seng Index to fall in September. It closed at 17,223 on 30th September, representing a drop of 13.7% from end-August and the largest monthly drop in nearly 11 years. The Shanghai A-share index declined by 5.5% over the same period, while the Dow Jones Industrial Average fell by 8.8%.

Stock Market Indices



Source: Bloomberg, data as of 30/9/2022

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