PRESS RELEASE

PR22/60

IMF Executive Board Concludes 2022 Article IV Consultation Discussions with the People's Republic of China—Hong Kong Special Administrative Region

FOR IMMEDIATE RELEASE

Washington, DC – March 8, 2022: On February 10, 2022, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation discussions[1] with the People's Republic of China—Hong Kong Special Administrative Region (SAR), and considered and endorsed the staff appraisal without a meeting on a lapse-of-time basis.[2]

Hong Kong SAR's economy is recovering strongly, with real activity increasing by 6.4 percent in 2021, as ample policy space allowed the enaction of swift and bold policy responses to address the unprecedented crisis emanating from multiple shocks, including the pandemic. In 2022, growth is expected to moderate to 3 percent, with a continued handoff from public to private demand facilitated by improving labor market conditions and a gradual re-opening of the border.

The financial system remains resilient supported by significant policy buffers, a strong external position, and strong institutional frameworks. Hong Kong SAR's financial system has continued expanding robustly even during the pandemic while maintaining its role as a major international financial center. The Hong Kong dollar continues to trade in a smooth and orderly manner within the Convertibility Zone. Housing prices, which declined by less than 1 percent in 2020 in terms of average annual prices, have increased by about 4 percent as of November in 2021.

Nevertheless, the balance of risks is tilted to the downside. In particular, pandemic related uncertainty, including renewed local outbreaks led possibly by new variants, could lead to a slower resumption in the flow of people, further weakening the recovery in private consumption. A slower-than-expected global recovery and sustained disruptions to global supply chains could reduce the flow of goods and derail the recovery. A sharp rise in global risk premia and a disorderly tightening in the monetary policy of major advanced economies could affect the flow of capital. Ample policy buffers and the strong external position should, however, help mitigate the adverse impact on financial stability and economic growth: fiscal and FX reserves stood at about 30 and 135 percent of GDP, respectively, as of November 2021.

---

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

Executive Board Assessment

In concluding the 2022 Article IV consultation discussions with Hong Kong SAR, Executive Directors endorsed staff appraisal as follows:

Outlook. The economy has recovered strongly supported by swift and bold policy responses, notably a large fiscal stimulus. The financial sector has remained resilient on the back of significant policy buffers, a strong external position, and strong institutional frameworks. However, the recovery remains unbalanced with private consumption lagging. The economic recovery is projected to continue in 2022 with a handoff from public to private demand, facilitated by a moderating pace of fiscal consolidation and a gradual re-opening of the border.

Risks. The balance of risks is tilted to the downside. Pandemic-related uncertainty could delay the resumption in the flow of people. A slower-than-expected global recovery and sustained disruptions to global supply chains could reduce the flow of goods and derail the recovery. A sharp rise in global risk premia, a disorderly tightening of monetary policy in major advanced economies, large housing market corrections, escalating U.S.-China tensions, and a shift of market confidence in Hong Kong SAR's status as a major international financial center could affect the flow of capital. Conversely, faster-than-expected border re-opening and global recovery and the development of the Greater Bay Area could improve growth prospects.

Fiscal policy. Fiscal policy should continue to support the recovery by returning to a balanced budget at a gradual pace, while focusing in the near term on providing more targeted support for low-income households, unemployed workers, and SMEs. Over the medium term, fiscal policy should strengthen its role as an automatic stabilizer and address structural challenges of population aging, high income inequality, and public housing shortage. A comprehensive tax reform that broadens the tax base while maintaining fairness and international competitiveness is needed to rebuild fiscal buffers.

Financial ties with Mainland China. The authorities should continue to strengthen systemic risk analysis of Mainland China-related credit risks, including by ensuring that the internal credit risk models used by Hong Kong SAR banks to determine the capital charges for exposures to Mainland Chinese borrowers, particularly those in the real estate sector with low credit ratings, are sufficiently forward-looking. Continued close monitoring of banks' significant exposures to non-bank Mainland Chinese entities and a periodic stress test of banks' large exposures—on top of the regular stress testing—would also help. As the financial ties are broadening to the cross-border use of the e-CNY in Hong Kong SAR, the potential implications from a more widely adopted e-CNY in Hong Kong SAR should be carefully studied.

Housing policies. The three-pronged approach—boosting housing supply, macroprudential measures, and stamp duties—to improving housing affordability and containing housing market risks remains valid. Housing supply should be increased, including by expanding land supply and expediting and streamlining the process for land identification and production. While the macroprudential stance for housing market should be maintained for now, the Council of Financial Regulators should take a lead in strengthening the regular surveillance and data collection on lending by non-bank lenders and the authorities should regularly assess the need to expand the regulatory perimeter to mitigate the leakages in macroprudential policies. The New Residential Stamp Duty, assessed to be a capital flow management measure and a macroprudential measure (CFM/MPM), should be phased out once systemic risks from non-resident inflows dissipate.

Financial sector policies. Financial policies should shift focus towards addressing solvency issues concerning corporates and individuals, as the recovery gains further momentum. The cut in the countercyclical capital buffer during the pandemic was appropriate but the Hong Kong Monetary Authority should stand ready to adjust it to the level consistent with updated systemic risk assessments. The ongoing efforts to further strengthen regulatory and supervisory frameworks are welcome, and further steps should be taken to enhance macroprudential oversight, including by adopting a more comprehensive and systematic approach to identify and address systemic risks. A consistent and cross-sectoral supervisory and regulatory framework is also critical to effectively address industry-wide fintech-related issues.

Exchange rate regime and external position. The Linked Exchange Rate System remains the appropriate arrangement as an anchor for economic and financial stability. The authorities should continue to preserve the rule of law and maintain the free flow of capital. Staff's preliminary assessment suggests that the external position in 2021 was broadly in line with the level implied by medium-term fundamentals and desirable policies.

Climate change. The updated action plan to achieve carbon neutrality before 2050 is welcome. To complement ongoing efforts, the government could consider introducing additional carbon pricing mechanisms to incentivize energy saving and green transportation. Climate-related risks should be carefully monitored and assessed by strengthening systemic risk analysis. Hong Kong SAR should play a key role in global efforts to mobilize private investment for green development by enhancing the green and sustainable finance ecosystem.

Hong Kong SAR: Selected Economic Indicators, 2017–26

	2017	2018	2019	2020	2021 (Proj.)	2022 (Proj.)	2023 (Proj.)	2024 (Proj.)	2025 (Proj.)	2026 (Proj.)
NATIONAL ACCOUNTS										
Real GDP (percent change)	3.8	2.8	-1.7	-6.1	6.4	3.0	3.0	2.9	2.8	2.8
Private consumption	5.5	5.3	-0.8	-9.9	6.2	4.8	4.8	4.6	4.3	4.1
Government consumption	2.8	4.2	5.1	8.1	4.0	0.6	2.0	2.3	2.3	2.3
Gross fixed capital formation	3.1	1.7	-14.9	-11.2	12.1	10.3	4.2	3.0	3.0	3.0
Inventories (contribution to growth)	0.4	0.0	-0.5	1.7	-0.1	-0.3	-0.3	-0.3	-0.3	-0.1
Net exports (contribution to growth)	-1.2	-1.5	2.1	0.3	-0.2	-1.9	-0.9	-0.8	-0.8	-0.8
Output gap (in percent of potential GDP)	0.1	0.1	-2.5	-6.8	-1.9	-1.2	-0.8	-0.5	-0.3	-0.1
LABOR MARKET										
Employment (percent change)	1.0	1.1	-0.4	-4.9	-0.2	2.0	0.5	0.6	0.7	0.7
Unemployment rate (percent, period average)	3.1	2.8	2.9	5.8	5.2	3.5	3.3	3.2	3.1	3.0
Real wages (percent change)	2.3	1.0	0.1	2.5	0.8	1.1	1.2	1.3	1.3	1.3
PRICES										
Inflation (percent change)										
Consumer prices 3/	1.5	2.4	2.9	0.3	1.6	2.1	2.3	2.4	2.5	2.5
GDP deflator	2.9	3.7	2.0	0.6	0.2	2.0	2.1	2.2	2.3	2.3
GENERAL GOVERNMENT										
Consolidated budget balance (percent of GDP) 1/	5.6	2.4	-0.6	-9.4	-3.7	-2.2	-1.5	-1.1	-0.7	-0.7
Revenue	23.3	21.2	20.8	21.0	21.6	21.7	21.9	21.8	22.0	22.0
Expenditure	17.7	18.8	21.4	30.4	25.3	23.9	23.3	23.0	22.7	22.7
Fiscal reserves (as of end-March, percent of GDP)	41.5	41.3	40.8	34.5	29.9	27.4	25.7	24.1	23.0	22.0
FINANCIAL										
Interest rates (percent, period average) 3/										
Best lending rate	5.0	5.0	5.1	5.0	5.0	...	...	...	...	...
Three-month HIBOR	0.9	1.8	2.1	1.1	0.2	...	...	...	...	...
10-year Treasury bond yield	1.6	2.2	1.6	0.8	1.2	...	...	...	...	...
MACRO-FINANCIAL										
Loans for use in Hong Kong SAR (excl. trade financing)	16.1	6.5	7.7	2.1	8.4	10.3	8.6	8.0	7.7	7.7
House prices (year-on-year percent change for last quarter)	13.7	5.8	3.4	-0.1	3.0	5.8	7.1	7.4	7.6	7.6
Credit-to-GDP gap 2/	20.6	12.5	21.2	23.9	11.5	12.2	9.6	6.2	2.7	0.0
Hang Seng stock index (percent change) 3/	36.0	-13.6	9.1	-3.4	-14.1	...	...	...	...	...
EXTERNAL SECTOR										
Merchandise trade (percent change)										
Export value	8.0	7.3	-4.1	-1.5	18.3	5.0	3.8	3.7	3.7	3.7
Import value	8.7	8.4	-6.5	-3.3	18.4	5.5	4.2	4.1	4.1	4.1
Current account balance (percent of GDP)	4.6	3.7	5.8	6.9	7.5	6.7	5.5	5.0	4.6	4.0
Foreign exchange reserves										
In billions of U.S. dollars (end-of-period)	431	425	441	492	500	508	516	525	537	553
In percent of GDP	126	117	122	142	135	131	126	122	119	116
Net international investment position (percent of GDP)	418	354	432	612	581	560	538	517	496	476
Exchange rate 3/										
Market rate (HK$/US$, period average)	7.793	7.839	7.836	7.757	7.773	...	...	...	...	...
Real effective rate (period average, 2010=100)	115.3	113.1	117.7	116.9	111.6	...	...	...	...	...

Sources: BIS,CEIC; HKSAR Census and Statistics Department; and IMF staff estimates.
1/ Before issuance and repayment of government bonds and notes.
2/ Based on loans for use in Hong Kong SAR, including trade financing.
3/ Actual values for 2021.