Macro Insights Weekly

A health-check on Hong Kong SAR

Group Research March 4, 2024

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- *To write-off Hong Kong is premature. It continues to rest on several constructive growth pillars, encompassing business-friendly rule of law, financial market depth, and a liberal immigration regime.*
- *Hong Kong's institutional strength is world class, with top decile ranking in many indicators.*
- *It's a hub for asset and wealth management. HK-domiciled funds have soared in recent years.*
- *Business ties between China and EU/ASEAN remain strong, helping Hong Kong's capital markets.*
- *The authorities have ramped up efforts to attract skilled immigrants.*
- *Economic and financial market returns have been disappointing, but Hong Kong's game is not over.*

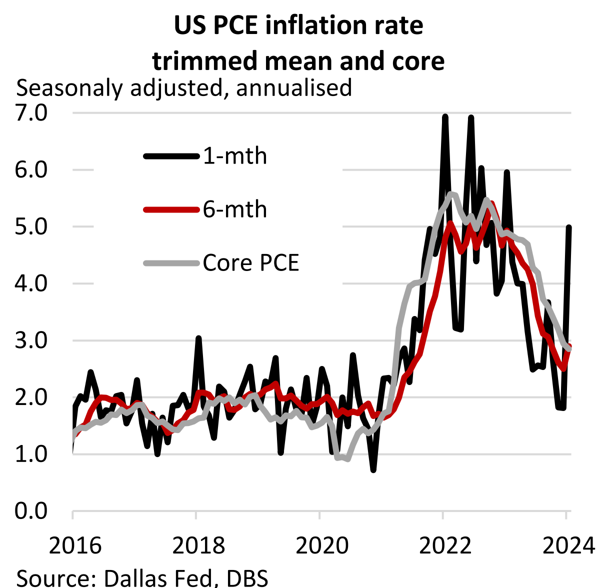
Key data release and events this week:

- *ECB is expected to keep rates unchanged.*
- *Uptick in inflation is anticipated in Taiwan, South Korea, and Philippines.*
- *Mainland China and Taiwan trade data are expected to decelerate in Feb due to Lunar New Year holiday.*

Chart of the Week: Firm core inflation in the US

Markets were sanguine with the January personal consumption expenditure (PCE) inflation data release last week. Both PCE (2.4%yoy) and core PCE (2.8%yoy) inflation readings were in line with expectations, helping support a mid-year rate cut scenario. But the Dallas Fed's trimmed mean PCE, an alternative measure of core, jumped by 5%yoy. This was driven by spikes in financial and hospital services, along with computer software and some beverage prices. Caution warranted.

US PCE inflation rate trimmed mean and core

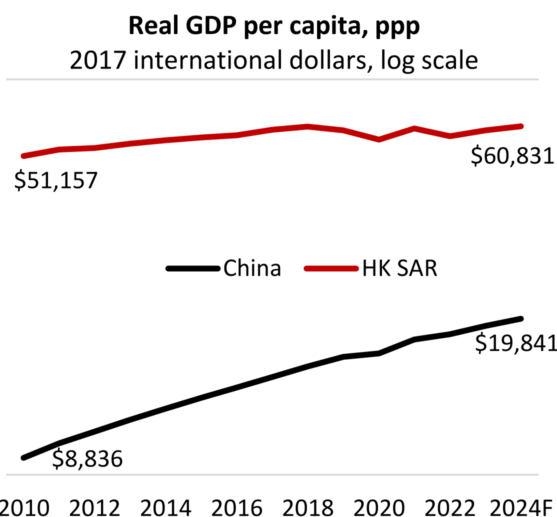


Source: Dallas Fed, DBS

Refer to important disclosures at the end of this report.

Commentary: A health-check on Hong Kong

It is tempting to write-off Hong Kong SAR. Years of stagnant growth, asset market selloff, pandemic shock, and geopolitical uncertainty have clouded the outlook of what has long been one of most dynamic financial centres of the world. Mainland China's economic duress has been spilling over to the island, while at the same time the relative wealth gap has been shrinking. Is Hong Kong really heading into a sunset, as many recent commentaries assert?



In an in-depth piece published recently, our China-HK economists point out that Hong Kong continues to rest on several constructive growth pillars, encompassing business-friendly rule of law, financial market depth, and a liberal immigration regime. To write-off Hong Kong, in our view, is premature.

Hong Kong's institutional strength is world class. According to the Rule of Law Index 2023 of the World Justice Project, Hong Kong was 23rd out of 142 places, on par with France (21st) and South Korea (19th), and above the US (26th). Strikingly, Hong Kong's ranking in anti-corruption ranking was 9.

Hong Kong's financial sector has grown and deepened over the years. It is a global hub for asset and wealth management. According to a KPMG survey, Hong Kong ranks highest in almost all asset management areas, including ease of onboarding, range of investment options, and investor protection. Regulators have also been reforming fund structures, making Hong Kong a more attractive location for fund domiciliation and origination. The number of Hong Kong-domiciled funds has grown by 20% to over 900 in the past 3 years.

While some American investors are shying away from Hong Kong, the trend has not broadened. Business ties between China and EU/ASEAN remain strong, while Hong Kong's role as the corporate gateway to China remains critical. There has been no change in the number of MNC corporate headquarters based in Hong Kong. Even the US-led effort to diversify regional supply chains has positive implication for Hong Kong, as the bulk of regional flows are intermediated through its capital markets.

The authorities have recognised the prevalence of headwinds, ramping up efforts to attract skilled immigrants. The government's Top Talent Pass Scheme has begun to attract both Mainland and foreign expatriates. Approximately 90,000 talents arrived through various talent admission schemes last year, far exceeding the government's annual target of admitting at least 35,000 talents. Of those who have arrived, 55,000 are approved applicants of the Top Talent Pass Scheme (TTPS). As a result, total labour force growth has stabilised. Yet another piece of evidence that Hong Kong's game is by no means over.

Taimur Baig and Samuel Tse

Key forecasts for the week

Event	DBS	Previous
Mar 4 (Mon)		
South Korea: industrial production (Jan)	9.0% y/y	6.2% y/y
Mar 5 (Tue)		
South Korea: GDP (4Q P)	2.2% y/y	2.2% y/y
Philippines: CPI inflation (Feb)	3.0% y/y	2.8% y/y
Thailand: CPI inflation (Feb)	-0.9% y/y	-1.1% y/y
Mar 6 (Wed)		
South Korea: CPI inflation (Feb)	2.9% y/y	2.8% y/y
Mar 7 (Thu)		
Eurozone: ECB refinancing rate	4.50%	4.50%
Taiwan: CPI inflation (Feb)	2.3% y/y	1.8% y/y
China: exports (Feb)	1.8% y/y	2.3% y/y
- imports	-0.5% y/y	0.2% y/y
- trade balance	USD114.6bn	USD75.3bn
Malaysia: BNM overnight rate	3.00%	3.00%
Mar 8 (Fri)		
Taiwan: exports (Feb)	1.1% y/y	18.1% y/y
- imports	-2.1% y/y	19.0% y/y
- trade balance	USD3.32bn	USD2.49bn

Central bank policy meetings

Bank Negara Malaysia (BNM) (March 7): We expect BNM to maintain its overnight policy rate (OPR) at 3.00% during its March meeting. Headline inflation remained contained at 1.5% YoY in January 2024, while 4Q23 real GDP growth was nudged down to 3.0% YoY from advance estimate's of 3.4% YoY, reflecting still soft growth conditions. An unchanged policy stance would likely remain supportive of the economy. Persistent currency depreciation vs the US dollar due to negative interest rate differentials does not provide room for easier monetary policy. BNM is likely to see little impetus to hike interest rates to stem currency weakness too. Higher rates would risk 'burdening the people', according to comments by Malaysia Second Finance Minister Amir Hamzah Azizan in parliament.

European Central Bank (ECB): The last mile of disinflation in the Eurozone is proving to be more challenging than earlier expected. February's inflation slowed to 2.6% yoy but was outpaced by core at 3.1% on simmering pressures in service costs. The ECB Governing Council will also table its staff projections this week. The forecast for 2024 is expected to be lowered, while the first projection for 2026 should see inflation head back to the 2% target. Policymakers are expected to monitor ongoing wage negotiations closely to gauge pipeline pressures, while staying on an extended pause at least until the summer.

Forthcoming data releases

China: Export growth is anticipated to decline from 2.3% YoY in December to 1.8% YoY in Jan-Feb. External demand from Mainland China and the rest of the world continues to encounter challenges due to high interest rates. Manufacturing PMI remained in contraction territory for the fifth consecutive month, with new export order PMI remaining weak. We expect import growth to decrease from 0.2% YoY in December to -0.5% YoY in January-February. The import PMI dropped from 46.7 in January to 46.4 in February, returning to the lowest level in the past 14 months.

Philippines: February inflation is expected to tick up to 3% yoy from 2.8% month before, within the central bank's target. Upside price pressures stem from the volatile food component including rice, meat, and fish, besides non-food items like fuel and utilities. Base effects are conducive for 1H24 which will help keep inflation within the target range notwithstanding simmering pressures. The BSP is expected to maintain a cautious stance, with delays in the US Fed's rate cut cycle also likely to keep the Philippine authorities from lowering rates prematurely.

South Korea: February's inflation data will be released this week. The government has signaled an expected uptick in February inflation, surpassing January's 2.8% YoY and potentially exceeding 3% YoY, primarily attributed to the Lunar New Year effects. Accordingly, the BOK is likely to maintain a neutral stance on monetary policy, resisting early rate cuts. However, close attention should be paid to post-LNY inflation patterns from March onward. Considering the softness in oil prices, deceleration in money supply, and labor market slack, there is a significant likelihood that inflation will ease to the mid-2% range in 3Q. This could potentially trigger a shift in monetary policy by the middle of the year.

Taiwan: February trade and inflation data will be released this week. We expect a deceleration in exports to 1.1% YoY from the 18.1% observed in January, attributable to a reduced number of working days during the Chinese New Year. Despite this, there are potential upside risks, as evidenced by South Korea's February exports, which beat expectations at 4.8% compared to the 18% reported in January. CPI inflation is poised for a rebound to the 2% mark in February, up from the previous month's 1.8%. The average inflation for the first two months of the year is expected to hover around 2%. With the policy rate standing at 1.875%, the likelihood of CBC rate cuts remains low in the near term.

Thailand: The negative headline inflation print likely extended into February 2024 at -0.9% YoY, in our view. Energy remained as the main price drag, due to the government's subsidies. The decline in raw food inflation could have narrowed, amid Lunar New Year festivities, while core inflation remained muted. The Bank of Thailand (BOT) will likely continue to look through the negative energy contribution. Yet, it is tough to ignore soft core inflation, which is below the authorities' 1-3% headline inflation target band.

Economics Team

FX: Cross currents amid convergences

Over the past few weeks, the **DXY Index and its components have ranged from converging monetary policy stances**. Like the US Federal Reserve, the European Central Bank and the Bank of England have signalled the potential end of the hiking cycles and called for patience in lowering interest rates. This narrative should be reaffirmed at Fed Chair Jerome Powell's semi-congressional testimonies on March 6-7 and the ECB governing council meeting on March 7. Apart from expecting Powell to sound less dovish, consensus has become less confident about Friday's US nonfarm payrolls falling below 200k in February. This week's events will decide if the DXY extends its rise above or falls below 104.

Policy rate outlook*

	FED	ECB	BOE	SNB
Feb 29	5.50	4.50	5.25	1.75
Mar	5.50	4.50	5.25	**1.50**
Apr		**4.25**		
May	5.50		5.25	
Jun	**5.25**	4.25	**5.00**	**1.25**
Jul	**5.00**	**4.00**		
Aug			5.00	
Sep	**4.75**	**3.75**	**4.75**	1.25
Oct		3.75		
Nov	4.75		4.75	
Dec	**4.50**	**3.25**	**4.50**	**1.00**

* based on interest rate futures, rounded to 0.25%
Sources: DBS Research, Bloomberg data

Interest rate futures see the Swiss National Bank lowering rates before its counterparts on March 21. Switzerland's CPI inflation returned to the SNB's 0-2% target in 3Q23. The consensus favours today's CPI slowing to 1.1% YoY in February from 1.3% in January. After trading above its 100-day moving average on February 13, **USD/CHF found support around 0.88.** To test 0.90 again, USD/CHF must first overcome the 200d and 300d MAs at 0.8830 and 0.8935.

Futures see the ECB cutting rates on April 11, before the Fed and the BOE in June. EU CPI inflation has been below its US counterpart since October. The Eurozone economy also stagnated compared to the resilient US economy. During the post-meeting press conference on Thursday, ECB President Christine Lagarde should stand by her comments on a likely rate cut in summer. On whether the ECB will ease before the Fed, Lagarde should assert the ECB's independence and data dependency, emphasizing how critical wage growth has become in assessing the timing of rate cuts. While encouraged that wage growth slowed to 4.5% YoY in 4Q23 from its 4.7% peak in 3Q23, the ECB will need the spring wage talks to ensure a declining trend. After recovering from a two-month low of 1.07 seen on February 14, **EUR/USD has been trapped between 1.0790 and 1.0870** or its 20- and 50-day moving averages, respectively. While EUR/CHF may test its 0.96 resistance again, EUR/GBP is confined in a 0.8540-0.8570 range.

GBP/USD has a downside bias within its 3-month range between 1.25 and 1.28. The UK's fundamentals are weaker than those of the US and the Eurozone. At the Spring Budget announcement on March 6, Chancellor of the Exchequer Jeremy Hunt will likely capitalize on the UK's technical recession to push for personal tax cuts. Futures do not see the Bank of England lowering rates at the March 21 and May 9 meetings. However, BOE Governor Andrew Bailey told the Treasury Select Committee on February 20 that the BOE expected CPI headline inflation to hit the 2% target in spring before rising again in the rest of the year. Bailey also emphasized that the BOE did not need headline inflation at 2% before cutting rates.

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