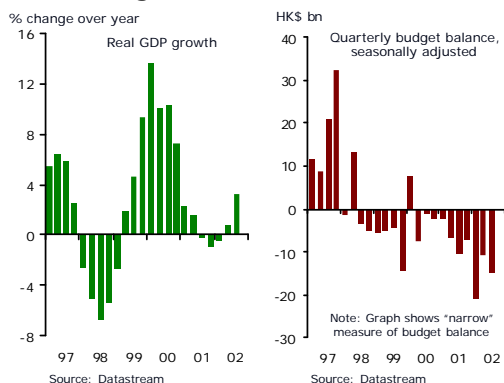
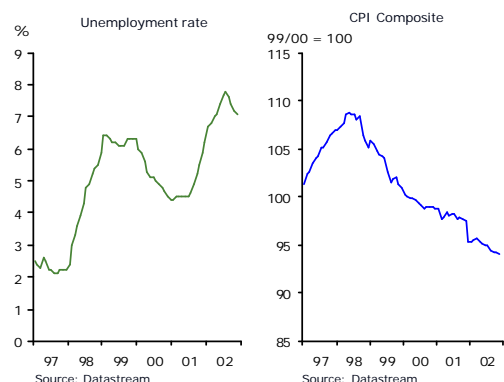


Country Update: Hong Kong

Signs of economic recovery at last, but budget deficit causes concern



Unemployment has peaked at last, but deflation continues



- Hong Kong's economy turned in a better-than-expected performance in the third quarter. GDP was 3.3% higher than a year earlier, with strong contributions from government consumption and net exports. Investment spending remains weak, but private consumption, on a seasonally adjusted basis, appears tentatively to be recovering.
- Despite a constitutional requirement that the budget be balanced over the cycle, it has been regularly in deficit since 1997, and the trend has worsened in the past two years. A government enquiry concluded that the deficit is structural, and as such it will not be eliminated by a recovery in economic activity. The budget for 2002/2003 contained no meaningful revenue-boosting measures, but small cuts to civil service salaries were approved in July.
- Unemployment rose substantially from early 2001 to mid 2002, peaking at 7.8%. In recent months it has declined to 7.1%.
- In November 2002 the Composite CPI was 3.6% lower than a year earlier, and 13.4% below its peak in May 1998. Deflation (and its effect in making credit expensive in real terms) has contributed to the sluggishness of the economy. Bank loans for use in Hong Kong declined by 3.4% over the year to November.

Economic data and debt statistics

| Hong Kong | 1997 | 1998 | 1999 | 2000 | 2001 | 2002e | 2003f | 2004f |
|-------------------------------------|------|------|------|------|------|-------|-------|-------|
| Economic growth (%) | 5.1 | -5.0 | 3.4 | 10.2 | 0.6 | 1.7 | 2.0 | 2.4 |
| Inflation (yr av, %) | 5.8 | 2.9 | -4.0 | -3.8 | -1.6 | -3.0 | -1.5 | 1.0 |
| Budget Balance (% of GDP) | 6.5 | -1.8 | 0.8 | -0.6 | -5.0 | -6.4 | -5.4 | |
| Current Account (% of GDP) | -3.5 | 2.4 | 7.1 | 5.4 | 7.3 | 7.5 | 9.6 | |
| External Debt (US\$ bn) | 40.4 | 48.3 | 38.2 | 42.2 | 45.9 | 49.3 | 54.1 | |
| Ext Debt/GDP Ratio (%) | 23.3 | 29.2 | 23.8 | 25.5 | 28.0 | 30.1 | 32.6 | |
| Ext Debt/Exports Ratio (%) | 13.9 | 18.7 | 14.8 | 14.2 | 16.3 | 17.1 | 17.7 | |
| Short term debt/Reserves (%) | 11.1 | 11.6 | 14.7 | 12.8 | 11.3 | | | |
| Debt Service Ratio (Paid) (%) | 1.5 | 2.5 | 2.1 | 2.4 | 2.5 | | | |
| Debt Service Ratio (Due) (%) | 1.5 | 2.5 | 2.1 | 2.4 | 2.5 | 2.6 | 2.6 | |
| Foreign Exchange Reserves (US\$ bn) | 92.8 | 89.7 | 96.2 | 107 | 111 | 111* | | |
| Import Cover (months) | 4.7 | 5.1 | 5.7 | 5.5 | 5.9 | | | |

*September 2002

Sources: IMF, Economist Intelligence Unit, ANZ Bank