Hong Kong Policy Address

Pro-growth policies not enough

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Hong Kong's Chief Executive Carrie Lam unveiled 2019 Policy Address yesterday. It proposed some policies to help local companies to alleviate the impact of economic downturn, but those measures seem inadequate in preventing the economy from further shrinking. SMEs focusing on local market will continue to suffer from the glum outlook. Housing policy is another focus. Property transaction may be moderately boosted by relaxation on mortgage, but all other policies are just old wine in a new bottle.

- **GDP may shrink in 2019.** Hong Kong is facing its first economic recession in a decade amid US-China trade war, shrinking global trade, and its local social events. During 2Q19 when the impact of social events was limited, HK GDP shrank 0.4% QoQ. Expect 3Q19 to slow further. The government has trimmed its full-year GDP growth forecast from 2-3% to 0-1%. IMF also slashed its GDP forecast for HK this week from its original estimate of 2.9% in Jan 19 to 0.3%. As the city's economic situation continues to darken, we expect the economy to shrink by 0.1% in 2019. If the social order gets back on track in 2020, the economy is expected to rebound by 0.6% YoY.

- **Retail sales slumped the most on record.** HK retail sales recorded the worst performance on record due to the disrupted tourism and local consumption. Retail sales in Aug 2019 slumped 23% YoY, extending the downtrend to seven consecutive months. The situation is even worse than 1998 and 2003. The outlook is still dim as it will take time to calm social unrest and rebuild the city's image as international trade and business hubs.

- **Job market feeling pain in certain sectors.** Despite HK's unemployment rate staying at 2.9% during Jun-Aug 19, the lowest in a decade, job market in some sectors is feeling the pain from deteriorating economy and facing layoff pressure, including retail, accommodation, food services and tourism.

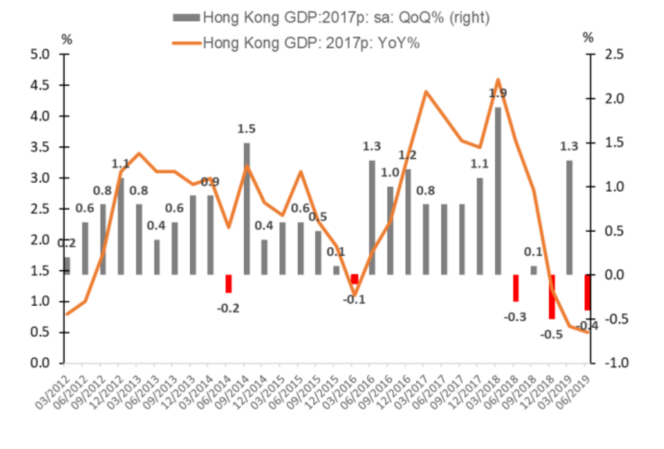
- **Pro-growth measures in Policy Address.** Policies to help local companies to expand opportunities across the border by offering tax incentives and simplified procedures and by grabbing more opportunities in "Belt and Road Initiative" and "Greater Bay Area" plans. To provide support to alleviate the impact of economic downturn on small business and people's livelihood. However, these measures seem inadequate in preventing the economy from further shrinking. Investor sentiment is hard to be restored and it will take time to identify and develop new growth drivers.

- **Housing policy – mortgage rule relaxed**. Mortgage restrictions are relaxed for homes under HK$10mn. First-time buyers can now borrow 90% on homes <HK$8mn. We believe this can help first-time buyers but their family income have to exceed HK$70k/month. Property transaction may improve but to a limited extent.

- **Land supply – new wine in old bottles.** Major plans of land supply are for long-term, and the policies are already heard before. Land resumption plan won't increase supply in the short term unless HK government offers an attractive price to land owners, who may take legal action against the plan. Changing the mix of public/private housing supply from 60/40 to 70/30 would reduce supply of private housing, thereby pushing up house price. Lastly, vacancy tax will be levied but it will mainly affect high-end market.

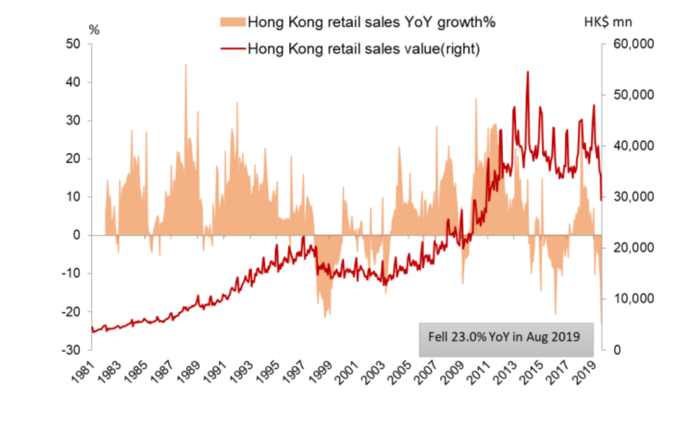
Focus Charts

Figure 1: HK is heading to first recession in a decade



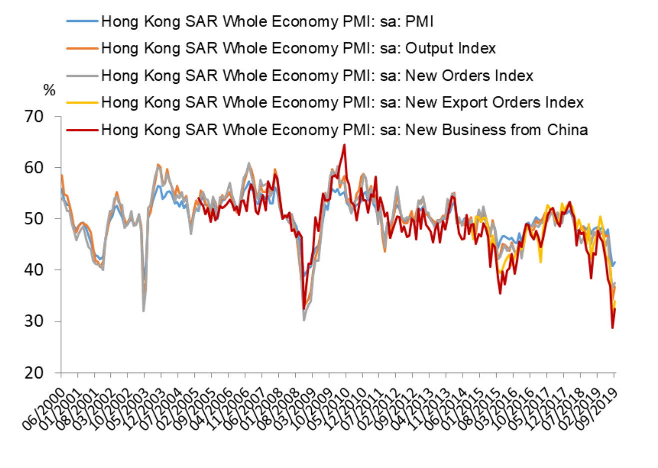
Source: CEIC, CMBIS

Figure 2: HK retail sales slumped the most on record



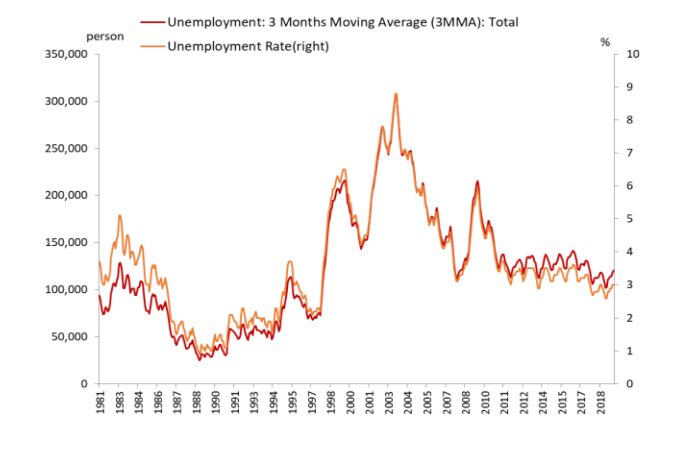
Source: CEIC, CMBIS

Figure 3: Whole economy PMI of HK dropped to record lows



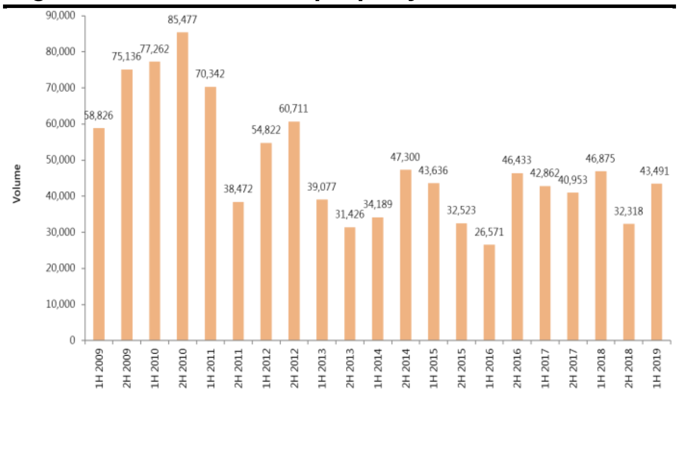
Source: CEIC, CMBIS

Figure 4: HK overall unemployment rate remained low while some sectors face layoff pressure



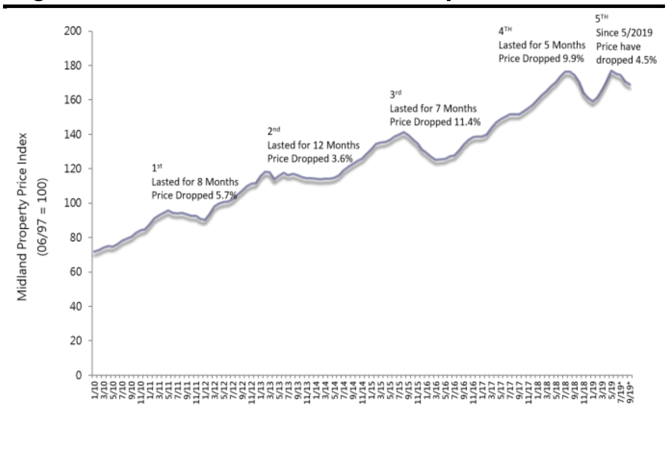
Source: CEIC, CMBIS

Figure 5: HK residential property transactions



Source: Midland Property Data and Research Centre

Figure 6: Fifth correction in house price in a decade



Source: Midland Property Data and Research Centre

Impact on HK stock market

Neutral on Hang Seng Index

Since the Policy Address does not have meaningful policies to solve the current social unrest, which is, along with US-China trade war, the key factors affecting the HK stock market, we believe the Policy Address has very little impact on the HSI.

Neutral to slightly positive on HK property & construction sectors

Relaxing mortgage rule would lend some support to house price, and increase home transactions to a limited extent, which are slightly positive for the property sector. On the other hand, increasing land supply would take years and the focus on public housing would reduce potential projects for developers and bring more competition.

We recap some key land/housing policies from this Policy Address below and their impact on related stocks:

■ Loosen mortgage restriction

Raise the cap on the value of the properties under the Mortgage Insurance Programme of the HKMC Insurance. For a first-time home buyer (i.e. a person without any residential property in HK at the time of application), the cap on the value of a property eligible for a mortgage loan of maximum cover of 90% loan-to-value (LTV) ratio will be raised from the existing HK$4mn to HK$8mn. For a property eligible for a mortgage loan of maximum cover of 80% LTV ratio (which may include a mortgage loan for self-occupied “flat for flat”), the cap on its value will be raised from HK$6mn to HK$10mn.

Stock implication:

- **Positive for property realty – Midland Holdings (1200 HK)** – on higher transactions.
- **Slightly positive for property developers**: increase buyers’ affordability, but note that 1) developers could offer second mortgages to buyers even before this mortgage rule relaxation; 2) most new flats are >HK$8mn.

■ Increase supply of public housing

Set aside HK$5bn to increase the number of transitional housing projects substantially to provide a total of 10,000 units within the next three years.

Invite the Hong Kong Housing Authority to explore the feasibility of redeveloping its factory estates for public housing.

Stock implication:

- **Positive for construction companies**.
- **Slightly negative for property developers**: increased competition from public housing.

■ Speed up housing supply (without changing total supply)

Propose HKHA to actively prepare for accelerating the sale of the existing 42,000 unsold flats in the estates under the Tenants Purchase Scheme.

Put up about 12,000 flats under the Home Ownership Scheme and Green Form Subsidised Home Ownership Scheme for pre-sale next year.

Propose legislation to levy "Special Rates" on vacant first-hand private residential units to encourage developers to expedite the supply of completed flats, in order to reduce hoarding.

Stock implication:

- **Negative for property developers:** increased competition from public housing; increased costs on unsold units.

■ Increase land supply for housing

Expedite planning work and then invoke the Lands Resumption Ordinance to resume three types of private land for developing public housing and Starter Homes:

- Privately-owned brownfield sites in the New Territories that may have development potential;
- private land which has been zoned for high-density housing development in statutory outline zoning plans, but without any development plans yet; and
- the urban private land located in Chai Kwo Ling Village, Ngau Chi Wan Village and Chuk Yuen United Village

Will soon announce details of the Land Sharing Pilot Scheme. At least 70% of the additional GFA gained should be allocated for public housing or Starter Homes. As such, land owners have to carve out part of their land and hand them over to the government for the said housing development, while the remainder of the site can be retained for private housing development.

Stock implication:

- **Neutral for property developers:** brownfield sites' value can be unlocked (positive), but would be rezoned for public housing rather than developers' own projects (negative); increased competition from public housing (negative); increased private housing projects from Land Sharing Pilot Scheme (positive).

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