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ROOM C-525

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BUFF/ED/93/15

February 2, 1993

Statement by Mr. Che on United Kingdom - Hong Kong  
Executive Board Meeting 93/16  
February 3, 1993

In 1992, Hong Kong's economy performed quite well on the basis of a strong rebound in 1991. A higher growth of 5 percent was solidly achieved in the context of a moderation of domestic private demand, as well as of the overall weakened demand in Western markets. Inflation as measured by the Consumer Price Index (A) moderated to about 9.4 percent, the lowest level since 1989. Trade development was equally impressive with both exports and imports attaining higher growth. The labor market remains flexible though not without fragility. On the whole, Hong Kong's economy was evidently in better shape in 1992.

The stronger growth momentum with reduced inflation in Hong Kong's economy can be attributed mainly to two factors. First of all, it is China's robust double-digit growth in 1992 that has a strong and decisive bearing on Hong Kong's satisfactory economic performance. The China element has once again demonstrated its powerful effects on Hong Kong's sustained growth. Secondly, the conventionally sound economic policy mix and environment were still primarily maintained by the Hong Kong authorities in 1992 despite some deviations. A strengthened recovery during the second half of the year in a few industrial countries, particularly the United States, has also been a positive factor for an outward-oriented economy such as Hong Kong's.

Nevertheless, during 1992, Hong Kong's economy was still disturbed by some apparently negative factors. One of the consequences was the sharp decline in Hong Kong's stock market at the end of the year. Business confidence has also been unavoidably affected. Consequent uncertainties were likely to have weakened an otherwise stronger growth for Hong Kong. Hong Kong began 1993 confronting additional challenges under these very special circumstances.

As my authorities are in broad agreement with the thrust of staff assessment, I would like to briefly reiterate our position on some major policy issues.

First, it is fair to say that the linked exchange rate system, adopted in 1983, has continued to make a positive contribution to bolstering economic and financial stability in Hong Kong. Needless to say, there is no perfect exchange regime, as any exchange arrangement reflects specific circumstances when it is adopted. The linked exchange regime is no exception. As Hong Kong is well into the transitional period, it is of vital importance to keep the exchange system stable in order to safeguard

the economic and financial stability in Hong Kong as well as the confidence of Hong Kong residents and investors. In this regard, we welcome the Hong Kong authorities' reiteration that they will continue to make efforts to sustain the linked exchange rate system. Also, we appreciate the authorities' adherence to the use of assets under the Exchange Fund mainly to stabilize the exchange rate.

Second, we note with grave concern that within a short period of time the total construction cost of the new airport has increased substantially. This will consequently pass a heavy and wasteful financial burden to the future H.K. Special Administrative Region and Hong Kong residents. Our view remains that there is plenty of room for containment of capital expenditures on the new airport. The Hong Kong authorities are urged to return to a more cost-effective package for constructing the new airport under the guidance of the 1991 Memorandum of Understanding.

Third, as the staff has rightly pointed out, given the constraint on monetary policy, fiscal policy should play a key role in containing domestic demand and repressing inflationary pressures. However, we are gravely concerned with the continued expansionary trend of fiscal policy in 1992 and beyond, resulting mainly from substantial investments in the new airport. The recent tendency to expedite spending is, in fact, eroding the soundness of fiscal policy. In this connection, we are in complete agreement with the staff that the importance of rationalizing budgetary expenditures should be stressed in order to avoid imparting additional stimulus to aggregate demand so long as the economy remains at full employment and inflationary pressures are strong.

Fourth, we have noted that in recent years the Hong Kong authorities have gradually strengthened both their influence in the money market and their supervisory mechanism over the banking sector, in light of changes in the economy and the financial sector. In this connection, we welcome the establishment of the Hong Kong Monetary Authority. We believe that maintaining a stable monetary management framework under the administrative structure is important for economic and financial stability.

Regarding prospects for Hong Kong's economy in 1993, we are confident that despite some uncertainties, the expectations for Hong Kong's economic growth will be optimistic. There are far more encouraging, as well as positive, factors which will continue to lend an even stronger back-up to Hong Kong's economy in 1993. What merits special mention here are the following points:

1. China's rapid growth with social stability has become the most important source of Hong Kong's sustainable export-led growth. In particular, the recent miraculous economic development in southern China continues to provide enormous opportunities to Hong Kong to widen, as well as deepen, its industrial transformation. Ties between these regions will become even closer.

2. China's recent announcement to move into a market-based economy and to further open the economy to the outside world will enable it to grow faster. Hong Kong will benefit as before from the strong growth of China's economy.

3. And, more importantly, the Chinese Government is committed as always to adhere to the Sino-British Joint Declaration and the Basic Law of the Hong Kong Special Administrative Region with the aim of guaranteeing a smooth transition and maintaining Hong Kong's stability and prosperity regardless of what will happen in the years to come. This is the most important factor for maintaining people's confidence in Hong Kong. In this context, we are confident that nothing can alter the bright long-term prospects for Hong Kong.

