SOUTH CHINA MORNING POST

30 Aug. 1989

Bank warns of threat of higher capital outflow

By GISELLE MILITANTE

THE spectre of increasing capital flight will continue to haunt Hongkong in the next few years, but the territory's high domestic savings are expected to cushion damaging effects on the economy.

According to the Standard Chartered Bank's Hongkong Economic Indicators released this month, events in China have severely shaken confidence in the territory.

It noted that a recent survey by the Federation of Hongkong Industries showed that 75 per cent of the sample intends to emigrate and 40 per cent was likely to reduce investments in the territory.

"Hongkong has to weather the storm of the latest confidence crisis so as to materialise its long run prosperity. Apart from the challenge of the so-called brain drain, the outflow of capital could be seen to become a major concern over the short to medium term," the bank said.

"Faced with the reality of an outflow of capital, Hongkong has to increase its domestic savings relative to investment or reduce investment relative to savings available."

During the past two decades, Hongkong had successfully weathered the capital drain through higher savings, which averaged about 32 per cent of gross domestic product (GDP), without much negative effect on economic growth.

This has enabled GDP to grow an average of nine per cent a year.

Capital outflow during the past five years averaged 4.4 per cent of GDP, still an acceptable figure from a historical perspective, according to the bank.

"In the national income identity, the balance of the current account is the counterpart of the saving-investment gap. An external account surplus will facilitate the outflow of capital without exerting a downward pressure on the exchange value of the Hongkong dollar or upward pressure on the local interest rates," the bank said.

"The ratio between flight capital and total export earnings of Hongkong, which indicates the affordability of a continued capital drain, stood at an average of 3.6 per cent during the past five years.

"The economic indicator argues that this is a very low figure as compared with the debt or service ratio of many indebted countries, showing that a persistent outflow of capital can be sustained and will not give rise to any serious damaging effect on Hongkong's external balance."

The bank noted, however, that this scenario would hold true in the future only if Hongkong could continue to boost its exports of services.

Hongkong could only trim its imports so much, while the potential of increasing manufactured exports was restricted by the slow growth of its labour force, it said.

The bank said Hongkong had become more of a service centre than a manufacturing base, with a substantial portion of its manufacturing activities already shifted to China.

The service sector had also grown in importance, accounting for more than 70 per cent of the territory's GDP.

"Net exports of services have enabled Hongkong to maintain a current account surplus in 15 years of the past 20," the bank said.

● Monitor, Page 12