Commentary

How the SARS Outbreak Will Affect Hong Kong's Economy

The severe acute respiratory syndrome outbreak will hurt Hong Kong's already-ailing economy in the short term, and it may even erode the city's status at the gateway to booming southern China for multinationals.

Hong Kong is suffering dramatic economic losses as the severe acute respiratory syndrome (SARS) crisis unfolds. Mass hysteria has gripped the city. Yet, different parts of the economy suffer in different ways. At the moment, SARS has barely affected imports, exports and foreign investment, but it has greatly convulsed the transport, wholesale, retailing and hotel businesses.

Immediate Economic Impact

SARS comes at a bad time for Hong Kong. It was already suffering economic pain, with historically high unemployment and slow economic growth. With manufacturing moving to mainland China and the real-estate industry still feeble after the 1997 to 1998 financial crisis, tourism and services are crucial to Hong Kong's economy — SARS has hit these two sectors the hardest. Tourism accounts for 6 percent of Hong Kong's gross domestic product (GDP). Traditionally, April is the start of the peak tourist season, but this April will likely prove a dismal season amid unprecedented travel advisories from the World Health Organization. Even if the outbreak is brought under control soon, businesses will need some time to return to normal — some restaurants report that their business is down by 65 percent because people do not want to risk eating out.

Economic forecasts of SARS's impact on Hong Kong's GDP growth range widely. Nearly all agree that SARS will shave at least 0.5 percentage points off Hong Kong's originally projected GDP growth for 2003. Some economists put this figure as high as 1.3 percentage points. However, at least one prominent investment bank (ING Groep) feels that the crisis has been hyped by the media and will soon come under control; it projects only about a 0.1 percentage point reduction in the original projected growth of the economy, and all of that in 2Q03.

The Long-Term Effects

The SARS outbreak will give global corporations a serious reason not to locate their Chinese operations in Hong Kong. Many base themselves in Hong Kong rather than China to expose themselves to less risk, and to take advantage of the city's attractions, advanced services and legal structure while they conduct
business with mainland China. However, Hong Kong's cramped living conditions favor the rapid spread of infectious diseases, which may soon broaden globally since Hong Kong is one of the world's favorite travel destinations and business connection points. For example, remember that other health crises used Hong Kong as a location from which to spread globally: The Hong Kong flu killed 700,000 people globally in 1968 and 1969 since it infected 30 percent of the world's population in less than nine months. Periodically, since 1997, local health authorities have also quelled eruptions of the avian flu, one of the few deadly diseases thought to directly jump from birds to humans. Multinationals may more heavily weight the risk of SARS-like outbreaks in their decisions about where to locate offices in China.

**Bottom Line:** Although Hong Kong acts as the gateway to booming southern China, the severe acute respiratory syndrome outbreak is adding to the city's economic woes. A number of multinationals are establishing headquarters in other parts of the region. More vibrant and assertive cities, especially Shanghai, are taking over some of Hong Kong's traditional regional leadership roles. Hong Kong's crisis of confidence continues.