HONG KONG MONETARY AUTHORITY
香港金融管理局

HALF-YEARLY MONETARY AND FINANCIAL STABILITY REPORT

September 2026

This Report reviews statistical information between the end of February 2026 and the end of August 2026, unless otherwise stated

Half-Yearly Monetary and Financial Stability Report
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1. Summary and overview

Two dominant themes defined global macro-financial developments during the period under review: the energy shock stemming from the Middle East conflict and the artificial intelligence (A.I.) investment boom. Both factors are inflationary, driving a pivot from anticipated rate cuts to rate hikes and pushing yields higher in advanced economies. On the growth front, the lift from the A.I. boom has largely offset the drag from the energy shock; however, these benefits have been unevenly distributed, depending on each country's position within the A.I. supply chain. Looking ahead, the global economy is projected to bend rather than break. Future prospects will be shaped by a combination of protracted Middle East tensions, tariff risks, tightening financial conditions, and questions regarding the sustainability of the A.I. boom.

The Hong Kong economy has demonstrated notable resilience against the energy shock, underpinned by its low energy intensity, low exposure to the Strait of Hormuz and prompt policy responses. This stability is further supported by strong trade activity related to the A.I. boom, improved service exports amid rising tourist arrivals, as well as stable consumption and investment in the private sector.

Hong Kong's exchange rate and money markets continued to trade in a smooth and orderly manner. While the local equity market recorded relatively weak performance, initial public offering (IPO) activities remained buoyant. Concurrently, the local debt market expanded steadily. Notably, Hong Kong's Renminbi (RMB) bond market benefited from lower RMB financing cost, the diversification advantage, and a series of key policy initiatives. The residential property market remained buoyant in the first half of 2026, underpinned by improved economic conditions and positive market sentiment. Meanwhile, the commercial real estate market showed signs of stabilsation. In the banking sector, loan growth turned positive, reversing the decline observed in the second half of 2025. The overall asset quality of the banking sector remained manageable; strong capital and liquidity position, combined with sufficient provisions, suggest that the banking sector is well positioned to withstand potential external and local shocks.

The external environment

The global macro-financial environment during the period under review was defined by two dominant themes: the energy supply shock stemming from the conflict in the Middle East and the A.I. investment boom. Both factors have intensified near-term inflationary pressures, driving a pivot from anticipated rate cuts to rate hikes and pushing yields higher in advanced economies. However, their impacts on growth have diverged significantly. While the energy

shock acts as a headwind, the A.I. boom has bolstered global demand. Overall, the boost from the A.I. boom has largely offset the drag from the energy shock, though the benefits have been unevenly distributed, depending on each country's position within the A.I. supply chain.

Regional performance has reflected these divergent forces. The US economy has demonstrated resilience, supported by robust A.I. investment, accommodative fiscal policy, rising oil exports, and strong spending by higher-income households. In contrast, economic activity in the euro area, the UK, and Japan has softened due to high energy costs and tighter financial conditions.

More recently, global financial conditions have tightened further. Long-term sovereign bond yields in the US, UK and Japan rose to their highest since 2007, reflecting inflation uncertainty and higher term premia. Meanwhile, major central banks have turned more hawkish. The US Federal Reserve (Fed) increased its policy rate by 25 bps in September, and its projections point to an additional 25 bps hike by 2026 year-end. Together with the rate hikes by the European Central Bank (ECB) and Bank of Japan (BoJ) in the same month, financial conditions are likely to tighten further in the near term.

Looking ahead, the global economy is projected to bend rather than break. Future prospects will be affected by multiple headwinds. A protracted Middle East conflict could sustain commodity price volatility and inflation while tightening global financial conditions. Long-term yields could rise further on continued heavy bond issuance. In addition, newly proposed US tariff measures and uncertainty over China-Europe trade tensions could possibly disrupt supply chains and weaken growth.

Furthermore, while the A.I. boom continues to support the global economic activity, it has generated increasing financial stability concerns. These include the rapid increase of debt finance to support massive A.I. infrastructure investment; the use of circular financing; growing exposures via private credit, derivatives and margin financing; and greater equity market concentration, particularly in East Asia. Fiscal vulnerabilities in major advanced economies also remain elevated, posing risks of higher global borrowing costs and further tightened financial conditions.

Asia Pacific (APAC) economies demonstrated resilience in the first half of 2026, primarily supported by the ongoing global A.I. investment boom that significantly lifted tech exports, manufacturing activities, and investment. The impact of the Middle East energy shock was also more benign than initially feared, thanks to adjustments in oil demand and supply in major economies, the deployment of commercial and strategic reserves, and targeted policy measures by governments in the region.

However, beneath this general resilience, economy-specific performance has diverged. Economies with weaker connections to the technology supply chain or insufficient buffers against the energy shock face greater challenges, characterised by rising inflationary pressures and downside risks to growth. Looking forward, APAC economies must closely monitor the evolution of geopolitical tensions in the Middle East, the emerging El Niño phenomenon and its impact on food security, and the dynamics of US tariffs under new arrangements.

In the first half of 2026, Chinese Mainland's real Gross Domestic Product (GDP) grew by 4.7%, falling within the annual target range. However, economic activity slowed down in the second quarter, driven by soft domestic demand. The economy continued to exhibit "K-shaped" divergence: surging exports and strong performance in new-economy sectors contrast sharply with weak domestic consumption and shrinking traditional industries. Box 1 examines Chinese Mainland's A.I.-related trade in greater detail. The housing market remained soft overall,

although top-tier cities performed relatively better. Inflation dynamics showed improvement, with the GDP deflator ending a consecutive 12-quarter period of negative growth in the second quarter, influenced by global energy shocks and the A.I. super cycle. Nonetheless, reflation remains narrow, and the pass-through to broader prices is limited. Looking ahead, the economy is expected to remain on track to meet its annual growth target of 4.5–5.0%. Despite lingering external challenges and fragile domestic demand, sustained innovations, industrial upgrading, and continued policy support are expected to underpin stable growth.

The domestic economy

In Hong Kong, the economy recorded solid growth in the first half of 2026, with real GDP increasing by 5.9% and 4.3% year on year in the first and second quarters, respectively. The economy has demonstrated notable resilience against the energy shock, underpinned by its low energy intensity, low exposure to the Strait of Hormuz, and prompt policy responses. This stability is further supported by strong trade activity related to the A.I. boom, improved service exports amid rising tourist arrivals, and stable performance of domestic activity. In particular, private consumption strengthened further, bolstered by solid consumer confidence and stable asset markets. In tandem, investment continued to expand in the first half of the year, underpinned by active property transactions and private sector capital spending. In addition, the labour market remained broadly stable, with the unemployment rate at 3.8% in August 2026. Consumer price inflation increased but remained moderate at 1.9% in August 2026.

Monetary conditions and capital flows

The Hong Kong dollar (HKD) exchange and money markets continued to trade in a smooth and orderly manner. In early March 2026, uncertainties arising from the Middle East conflict prompted investors to unwind short HKD positions, temporarily driving the HKD stronger. Nonetheless, this was subsequently offset by carry trade activities, incentivised by HKD interest rates moving below their US dollar (USD) counterparts, which drove the HKD weaker. Market fluctuations were largely driven by capital flows related to Southbound Stock Connect and other capital market activities.

While Hong Kong Interbank Offered Rates (HIBORs) generally track their USD counterparts under the Linked Exchange Rate System, shorter-tenor rates are also influenced by local supply of and demand for HKD funding. Reflecting shifts in seasonal and capital market-related funding demand, short-term HIBORs eased in early March before generally firming thereafter. Box 2 examines how Fast Interface for New Issuance (FINI) has reduced IPO-related interbank transfers, thereby dampening the impact of large IPO subscriptions on overnight HIBOR.

Going forward, heightened geopolitical risks, the ongoing military conflict in the Middle East, and elevated uncertainty regarding the US trade policy and the sustainability of the A.I. investment boom may increase fund flow volatility. Nonetheless, with ample foreign exchange reserves and robust financial system, Hong Kong is well positioned to withstand these volatilities without undermining financial stability.

Asset markets

During the review period, global equity markets recorded gains, but experienced significant volatility as the Middle East conflict persisted. While continued optimism over A.I.-related developments provided support to global equity markets in the first half of 2026, concerns over the sustainability of massive A.I. capital expenditure triggered a sell-off in A.I.-related hardware and infrastructure companies in July, contributing to volatility in global equity

markets. In Hong Kong, the local equity market recorded weaker performance in the second quarter of 2026, but rebounded notably in July. Looking ahead, the outlook for global equity markets remains highly uncertain. The Middle East conflict and vulnerabilities associated with massive A.I. capital expenditure will remain key sources of risks, while uncertainty over the interest rate paths in major advanced economies and persistent geopolitical and trade tensions could also trigger volatility. For Hong Kong, market sentiment will also be shaped by the economic growth and technological developments in the Chinese Mainland.

In the bond market, yields on long-term US Treasury Notes increased amid rising inflation concerns and risks to long-term US fiscal sustainability. While the yields on HKD Hong Kong Special Administrative Region Government Bonds and corporate bonds also rose, they remained lower than yields on USD bonds of comparable maturities.

A puzzling development in the global bond market is that the average spread for high-yield bonds has remained tight, staying below the historical average despite volatile global financial markets. Box 3 explores this phenomenon by linking it to the rapid growth of the private credit market, and discusses its implications for financial stability.

In the first half of 2026, the issuance of HKD debt securities grew by 11.6% year on year, with issuers outside Hong Kong being the primary contributor. Meanwhile, the issuance of offshore renminbi (CNH) debt securities rose by 60.5% year on year during the first half of 2026. Looking ahead, the lower financing cost and investors' diversification demands are expected to continue supporting HKD and CNH debt securities issuance. Over the longer term, continued large-scale HKD debt securities issuances in the public market could help deepen the HKD debt market, while policy measures to promote RMB internationalisation will further support the development of the CNH debt market in Hong Kong. During the review period, several policy initiatives were introduced to foster the development of Hong Kong's debt market, covering green and sustainable finance, technological innovations, and market infrastructure improvement.

The residential property market remained buoyant in the first half of 2026, underpinned by improved economic conditions and positive market sentiment. Looking ahead, the housing market outlook remains subject to risks and uncertainties, including those stemming from the US interest rate path. That said, the robust domestic economy, coupled with the sustained net inflow of talent and overseas students, should continue to support housing demand in the near term. Meanwhile, the commercial real estate (CRE) market showed signs of stabilisation. In particular, vacancy rates for both grade A offices and retail premises in prime districts improved further.

Banking sector performance

The aggregate pre-tax operating profit of retail banks grew by 20.4% year on year in the first half of 2026, driven by higher net interest income, income from fees and commissions, and income from investment held for trading. This growth was partially offset by the decline in income from foreign exchange and derivatives operations. As a result, banks' return on assets rose to 1.40% in the first half of 2026, up from 1.27% in the same period last year.

The Hong Kong banking sector remains liquid and well capitalised. The average Liquidity Coverage Ratio of category 1 institutions reached 150.5% in the second quarter of 2026, well above the statutory minimum requirement of 100%. The total capital ratio of locally incorporated authorized institutions (AIs) stood at 24.2% in the second quarter of 2026, significantly

exceeding the international minimum requirement of 8%. The asset quality of the banking sector remained manageable and showed signs of improvement, with the classified loan ratio for all AIs declining to 1.82% in the second quarter of 2026.

Financial health among Hong Kong-listed non-financial corporates also showed signs of improvement, reflected by a higher weighted average interest coverage ratio and lower corporate leverage. Despite these recent improvements, their longer-term resilience will depend partly on their ability to adopt new technologies to enhance efficiency and support revenue growth. Box 4 examines this issue by drawing on the recent experience of digitalisation adoption among Hong Kong corporates.

Looking ahead, several downside risks, including the spillover risk from debt vulnerabilities in A.I. firms, ongoing geopolitical tensions in the Middle East, and uncertainty over the future path of US interest rates, could pose challenges to the Hong Kong banking sector. Banks are advised to remain vigilant in assessing the impacts of these risk factors on the asset quality of their loan portfolios.

The Half-yearly Report on Monetary and Financial Stability is prepared by the staff of the Research Department of the Hong Kong Monetary Authority

2. Global setting and outlook

2.1 Advanced economies

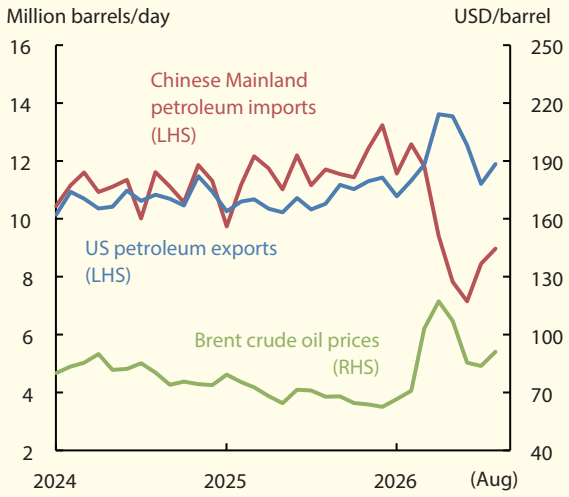
Two overarching forces have shaped the global macro-financial environment in the first half of 2026: the energy supply shock stemming from the ongoing Middle East conflict and the boom in artificial intelligence (A.I.)-related investment. With the ongoing stalemate in US-Iran negotiations, the full restoration of navigation through the Strait of Hormuz (SOH) remains uncertain. Disruptions to energy supply chains continue to exert widespread impacts, including higher energy and fertiliser prices, supply-chain frictions and elevated risk premia. These factors are likely to add inflationary pressures and weigh on global growth prospects.

Meanwhile, the A.I. investment boom has continued to support global demand. Economies that are more integrated into the A.I. supply chain have generally benefited more from this upturn on the growth front. However, the surge in investment has also contributed to price pressures by increasing demand for chips, electricity, and skilled labour.

Taken together, the energy shock and the A.I. investment boom are both inflationary. Yet, their divergent implications for growth — the former acting as a headwind and the latter providing support — have contributed to divergence across economies.

During the period under review, the energy shock led to a significant increase in energy prices and headline inflation. However, the damage proved less severe than initially feared for several reasons. First, the geopolitical tensions fluctuated without escalating into a full-scale conflict, causing short-term volatility rather than a persistent upward trend in energy prices. Second, part of the reduction in oil shipping via the SOH was offset by the deployment of commercial and strategic oil reserves. In addition, an increase in US oil exports and a significant reduction of Chinese Mainland's oil imports helped contain the demand-supply imbalance (Chart 2.1). That said, the impact has differed across jurisdictions, depending on the energy intensity of the economy, reliance on oil imports (particularly exposure to the SOH), inventory levels, and the scope for fiscal policy response. Meanwhile, each economy's position in the technology value chain has contributed to divergent performance in economic activity and growth.

Chart 2.1
Crude oil prices, petroleum exports from the US and imports by the Chinese Mainland

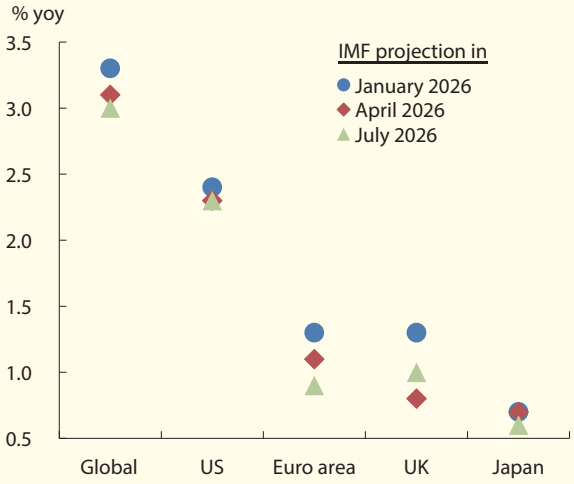


Sources: CEIC, China Customs and US Energy Information Administration.

In the US, disruptions to the energy supply chain have fuelled inflation. Brent oil prices reached a three-year high in April 2026, contributing to an increase in US headline inflation to 4.2% in May before easing to 3.4% in August 2026. Nevertheless, the US economy has remained relatively resilient, supported by increased oil exports, the A.I.-led investment boom, accommodative fiscal policy, and easing financial conditions earlier in the year. The latest International Monetary Fund (IMF) projections suggest that US gross domestic product (GDP) growth is likely to remain solid despite the

impact of the Middle East conflict, with the smallest downward revision in growth forecasts among advanced economies (Chart 2.2).

Chart 2.2
Real GDP growth projections for 2026 in major advanced economies



Source: IMF.

Due to upside inflation risk, the US Federal Reserve (Fed) increased the federal funds target rate by 25 basis points in September. Relative to the June projection, most Federal Open Market Committee participants shifted in a more hawkish direction. The latest dot plot indicated an additional tightening of 25 basis points by the end of 2026 compared with September, broadly inline with market pricing.

In the euro area, economic activity moderated in the first quarter of 2026 amid the energy shock stemming from the Middle East conflict, before rebounding in the second quarter. While broader financial conditions remained supportive by historical standards, bank lending conditions tightened following a cumulative 50-basis-point policy rate hike of the European Central Bank (ECB) in June and September. Following the ECB's policy rate increase, the growth outlook remained subdued, and the IMF revised down its GDP growth projection (Chart 2.2). Similar headwinds are facing the UK economy. Meanwhile, the Japanese economy experienced moderated growth with sustained inflationary pressure. This situation was compounded by the Japanese yen's depreciation to a four-decade low before the joint market intervention by the US and Japan in late July 2026. Although this depreciation supports exporters, it increases import costs and inflation risks, prompting the Bank of Japan to raise its policy rate by 25 basis points in September.

More recently, global financial conditions have tightened. Global bond markets came under intense pressure in August amid heavy sovereign issuance, reduced official absorption and uncertainty over energy-related inflation. 30-year sovereign bond yields in the US, the UK and Japan reached their highest since 2007. In Europe, fiscal loosening in Germany has added to Bund supply and elevated gilt yields have squeezed the UK's fiscal headroom, while in Japan the BoJ's hawkish turn has flattened the yield curve. In the US, higher term premia have pushed up the long-dated Treasury yields. Although the US Treasury expanded its liquidity-support buyback operations from September, yields remained elevated. Together with more hawkish stance by major central banks, global financial conditions are likely to tighten further in the near term.

Looking ahead, the global economy will likely bend but not break. The global economic outlook remains affected by multiple headwinds. In particular, geopolitical tension and consequent uncertainties will persist. The ongoing Middle East conflict could prolong commodity price volatility, continue to disrupt supply chains, exacerbate inflationary pressures, and tighten financial conditions. The risk is likely to intensify if the SOH blockade persists, given that declining inventory levels have diminished the buffer and the room for adjusting demand and supply has become more limited. Meanwhile, trade uncertainty stemming from the US will not ease off, despite the invalidation of the executive tariffs under the International Emergency

Economic Powers Act and the expiration of Section 122 temporary tariffs. Average US tariffs have remained at an elevated level with the introduction of Section 301 tariffs on 60 economies, which set additional duty rates of 10% or 12.5%.[1] Tariff escalation with Canada and the expiry of the US-China trade truce in November add to the uncertainty. Separately, trade tensions between China and Europe have risen amid a record bilateral trade imbalance, leading to tariff hikes in certain sectors;[2] an escalation could disrupt global supply chains and further weigh on Europe's already subdued growth outlook.

While the A.I. investment boom continues to support the global economy, it has also generated increasing concerns in financial markets. As major tech firms sustain massive investments in A.I. infrastructure, global demand for semiconductors has reached record highs. Leading chipmakers have reported robust earnings growth, though it is still too early to determine whether and how A.I. deployment will increase productivity in the economy and the earnings in other sectors. Concerns about financial vulnerabilities arise from a shift in funding sources from cash flows to debt financing, especially via private credit or circuit financing; increasing concentration risk in the equity market;[3] and rising relevance of cross-border derivatives and margin financing. A sudden market correction could have an amplified negative feedback loop that may precipitate broader macro-financial instability.

The economic and financial market outlook is also complicated by a potential shift in the monetary policy frameworks of major central banks. Higher inflation and inflation expectations have reversed the monetary easing cycle into hikes, yet the path and strategy remain uncertain. The new Fed Chairman has launched external task forces to overhaul the Fed's monetary policy framework, focusing on communication, balance sheet policy and inflation frameworks. Meanwhile, the ECB has also shifted its strategy back to basics, relying on conventional interest rate tools and dropping long-term forward guidance. How these changes will affect monetary policy decisions and the interactions between financial markets and monetary authorities remains to be seen.

Meanwhile, fiscal sustainability risks in major advanced economies remain a source of concern, amid high public debt levels, persistent fiscal deficits and limited progress in fiscal consolidation. In the US, elevated debt levels, together with the possibility of high-for-longer interest rates in the face of renewed inflationary pressures, could lead to a further increase in debt servicing burdens over time. Continued sizeable issuance of US Treasuries to meet financing needs may also place upward pressure on global borrowing costs and global financial conditions could be further tightened.

2.2 Asia Pacific economies

In the first half of 2026, APAC economies registered solid growth despite the Middle East conflict and the associated energy shock. The region's resilience was largely underpinned by the ongoing global A.I. investment boom, which boosted tech exports and spurred growth in related manufacturing activities and infrastructure investment. Meanwhile, beneath the general resilience lies a notable "K-shaped"

[1] The investigation concluded that all 60 economies failed to impose and effectively enforce a forced labour import prohibition. Although 14 economies (e.g. Canada, Mexico and the European Union (EU)) faced the same tariff rate as a temporary measure under Section 122 (i.e. 10%) imposed in February 2026, the other economies (e.g. China, Japan and South Korea) faced a higher tariff rate of 12.5%. In addition, the US administration imposed a 25% tariff on certain imports from Brazil and a 50% tariff on selected imports from Canada in late July.

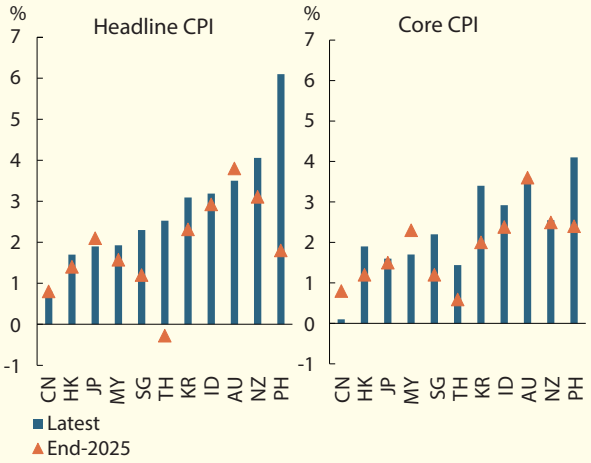
[2] The EU implemented anti-subsidy tariffs ranging from 17% to 35% on Chinese electric vehicles, prompting counter-probes from Beijing on European dairy, pork and brandy

[3] This risk is particularly pronounced in East Asian economies, where a limited number of chipmakers constitute a significant portion of market indices.

divergence across economies, depending on their exposure to the global energy shock and their position in the technology value chain.

The divergence in economic performance is in part due to the uneven impact of the energy shock. At the global level, the impact of the Middle East conflict proved more benign than initially feared, cushioned by adjustment in oil supply and demand in major economies. Still, APAC is among the most vulnerable to the energy shock, with some economies having high exposure to oil imports from the SOH (e.g. Japan, South Korea and Taiwan). Large strategic oil reserves were helpful to cushion the shock. In addition, various policy measures deployed by regional governments, such as fiscal subsidies, purchase limits, supply rationing, and more diversified oil procurement strategies, helped stabilise domestic demand and sustain operations in critical sectors. Nonetheless, inflationary pressures intensified across the region, with the impact varying depending on the exposure of each economy and the size of their cushion factors (Chart 2.3).

Chart 2.3
Asia Pacific: Headline and core consumer price index inflation

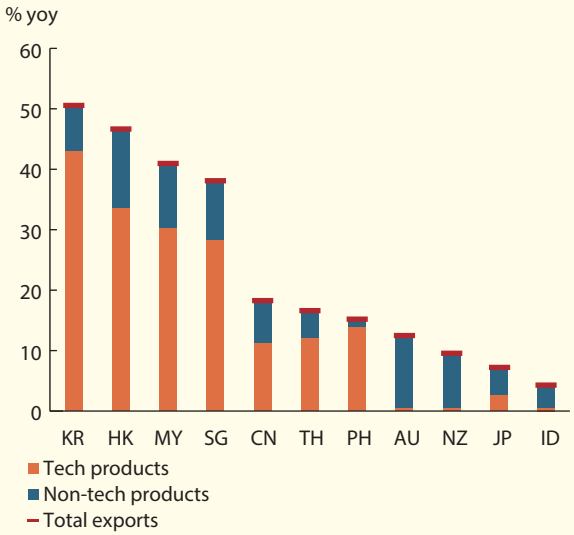


Notes:
1. CPI = Consumer price index, AU = Australia, CN = Chinese Mainland, HK = Hong Kong, ID = Indonesia, JP = Japan, KR = South Korea, MY = Malaysia, NZ = New Zealand, PH = The Philippines, SG = Singapore, TH = Thailand
2. The latest observation refers to Q2 2026 for NZ, July 2026 for AU, and Aug 2026 for all other economies.

Source: CEIC.

Divergent performance also reflects the position of each economy in the global A.I. supply chain. South Korea and China (including the Chinese Mainland, Hong Kong and Taiwan) are deeply tied to the A.I. supply chain and have captured outsized gains, leading to sharp increases in exports (Chart 2.4) and equity valuations (in South Korea and Taiwan). By contrast, those economies with little connection with the A.I. supply chain have generally experienced subdued performance.

Chart 2.4
Asia Pacific: 2026 export growth with breakdown by product type



Notes:
1. AU = Australia, CN = Chinese Mainland, HK = Hong Kong, ID = Indonesia, JP = Japan, KR = South Korea, MY = Malaysia, NZ = New Zealand, PH = The Philippines, SG = Singapore, TH = Thailand
2. Figures are January–June for PH and SG, and January–July for all other economies.
3. "Tech products" refer to products falling under Harmonized System codes 8419, 8470–8473, and 85.

Sources: CEIC, International Trade Centre (ITC) and HKMA staff calculations.

While the ongoing strength in global tech demand may continue to support the resilience of APAC economies, significant near-term vulnerabilities remain, given the risks and uncertainties outlined in preceding paragraphs.

In particular, regional inflation faces substantial upside pressure from two key catalysts. First, the ongoing Middle East conflict may continue to elevate prices for fuel-sensitive consumer price index (CPI) items, with risks of these pressures transmitting to broader CPI through second-round effects. Second, the emerging super El Niño phenomenon poses additional risks through weather disruptions, which, combined with fertiliser supply constraints, will ripple through food supply chains and exert upward pressure on food prices.

In addition, prolonged volatility in commodity prices and further increase in long-term yields across major advanced economies may weigh on regional capital flows and foreign exchange stability. This, coupled with rising inflationary pressures, could prompt central banks across the region to adopt a more aggressive tightening stance (Chart 2.5), potentially slowing economic growth, particularly in economies that have limited exposure to the technology sector, larger external financing needs, and higher inflation pass-through. Moreover, although the US has raised tariff rates on several regional economies following its Section 301 investigation, uncertainty over US trade policy remains heightened, further complicating the region's growth outlook.

Chart 2.5
Asia Pacific: Policy interest rate moves since 2025

	Number of rate cuts / hikes in 2025	2026									Current rate (%)
		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	
AU	3 cuts	-	hike	hike	-	hike	hold	-	hold	-	4.35
CN	1 cut	-	-	-	-	-	-	-	-	-	1.40
ID	5 cuts	hold	hold	hold	hold	hike	2 hikes	hold	hold	hold	5.75
JP	2 hikes	hold	-	hold	hold	-	hike	hold	-	hike	1.25
KR	2 cuts	hold	hold	-	hold	hold	-	hike	hike	-	3.00
MY	1 cut	hold	-	hold	-	hold	-	hold	-	hold	2.75
NZ	6 cuts	-	hold	-	hold	hold	-	hike	-	hike	2.75
PH	5 cuts	-	cut	hold	hike	-	hike	-	hike	-	5.00
TH	4 cuts	-	cut	-	hold	-	hold	-	hold	-	1.00

Notes:

1. AU = Australia, CN = Chinese Mainland, ID = Indonesia, JP = Japan, KR = South Korea, MY = Malaysia, NZ = New Zealand, PH = The Philippines, TH = Thailand
2. "-" indicates months with no monetary policy meeting or policy interest rate decision.
3. Based on data as of 23 September 2026.

Sources: CEIC, central bank websites and HKMA staff calculation.

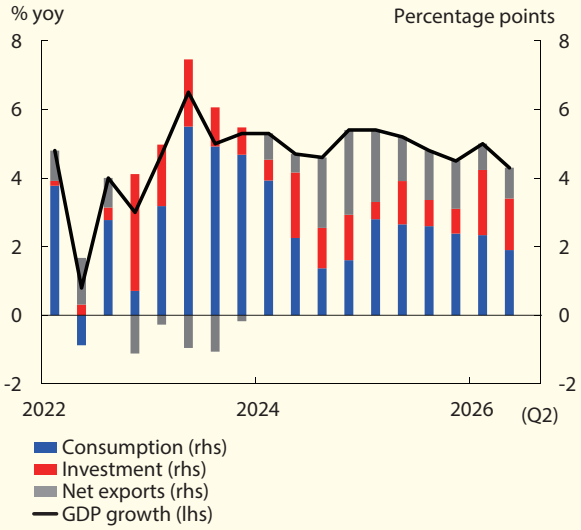
2.3 Chinese Mainland

Economic performance

Real GDP growth in the Chinese Mainland eased to 4.3% year on year in the second quarter of 2026, down from 5.0% in the first quarter. This deceleration primarily reflected softer domestic demand, while net exports remained resilient (Chart 2.6). Consumption growth moderated, due to the scaling back of the trade-in programme and the payback effect from front-loaded spending in the previous year; however, services outperformed goods. Fixed asset investment contracted in the second quarter, weighed down by a property market consolidation and a reversal in infrastructure investment amid weaker fiscal support. The contribution of net exports to GDP growth increased slightly in the second quarter despite having narrowed from 2025. In nominal terms, both merchandise exports and imports accelerated, supported by buoyant global demand for technology and A.I.-related products. Box 1 examines these A.I.-related trade in greater detail, suggesting its strength stemmed primarily from price increases rather than volume growth. In addition, the energy shock arising from the Middle East conflict boosted the Chinese Mainland's green exports, such as electric vehicles.

Taken together, the real economy expanded by 4.7% year on year in the first half of 2026, still within the official growth target range of 4.5%–5.0% for the year. However, various activity and sectoral indicators revealed an underlying "K-shaped" divergence — strong supply versus weak demand, resilient exports versus soft domestic consumption, and vibrant new-economy sectors versus shrinking traditional sectors such as housing.

Chart 2.6
Chinese Mainland: Contribution to GDP growth by demand component



Sources: National Bureau of Statistics of China (NBS), CEIC Data (CEIC) and HKMA staff estimates.

Outlook and risks

The economy is expected to remain on track to meet its annual growth target amid continued policy support.[4] The authorities have pledged to strengthen counter-cyclical adjustments through prioritising faster deployment of existing fiscal resources, while the People's Bank of China (PBoC) is set to maintain a moderately loose monetary policy stance.

In a challenging external environment, the economy has demonstrated strong resilience, and advanced from a large to a strong manufacturing power. Bright spots in the economy include A.I. models, humanoid robots, semiconductors, new energy and green transition, and the list continues to expand. Sustained innovations, industrial upgrading, and the expansion of new-economy sectors are expected to underpin stable growth.

However, the growth outlook is affected by several uncertainties and risks. These include the evolving conflict in the Middle East, the sustainability of the A.I. boom, uncertainties surrounding US tariffs[5] and policy interest rates, potential trade tensions with the EU, and the headwinds from property market. Current market consensus forecasts a growth rate of 4.6% for the year.

Driven by global energy shocks and the A.I. super cycle, inflation dynamics improved in the first half of 2026 (Chart 2.7), although reflation remained narrow. Producer price index (PPI) inflation rose to a recent high in June, fuelled by higher prices in energy, chemicals and certain A.I.-related industrial metals. However, weak consumer demand generally limited downstream pass-through,[6] potentially pressuring corporate margins. Headline consumer price index (CPI) inflation ticked up from 2025 but remained relatively soft at around 1.0% year on year in the first eight months of 2026, as lower food prices partially offset the impact of higher gasoline prices. After declining for 12 consecutive quarters, the GDP deflator turned positive in the second quarter of 2026. Meanwhile, the headline unemployment rate edged up to 5.3% in August 2026, with the youth unemployment rate for the 16–24 age group picking up to 18.9% amid the traditional graduation season.

Importantly, while the global energy shock and the A.I. boom have affected the Chinese Mainland, the economic and policy cycle in the

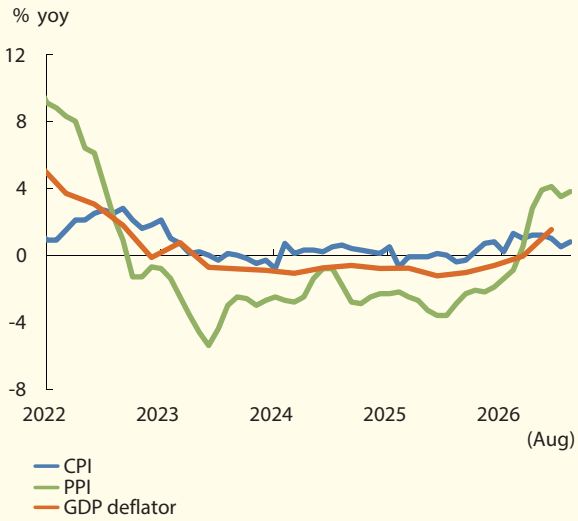
[4] For example, the Central Government announced new consumption and tourism plans for the National 15th Five-Year Plan (FYP) period, targeting total retail sales of RMB 60 trillion and domestic tourism spending of RMB 7.7 trillion by 2030. Other ongoing measures include the "Six Networks" investment and "A.I. plus" initiatives.

[5] The China-US tariff truce agreed in October 2025 is due to expire on 10 November 2026. Separately, the US Trade Representative has imposed a new 12.5% tariff on several economies, including the Chinese Mainland, following Section 301 investigations. Meanwhile, China and the US are seeking to reduce tariffs on certain agricultural products following the Xi-Trump summit held in mid-May. Overall, the China-US trade relationship will not deteriorate in a baseline scenario, as the top leaders agreed on a framework of a constructive relationship of strategic stability.

[6] There are exceptions, such as vehicle fuels and IT devices like mobile phones.

Chinese Mainland remains largely domestically driven. Despite the jump in PPI inflation, the pass-through to consumer prices has been limited. Consequently, the PBoC has maintained its monetary policy stance, and government bond yields have remained stable — in contrast to the upward trend in advanced economies. The low correlation between the Chinese Mainland and advanced economies is not a new phenomenon; it reflects structural economic differences, distinct financial market divergence, and policy-driven cycles.

Chart 2.7
Chinese Mainland: Inflation and GDP deflator



Note: The GDP deflator is reported on a quarterly basis, while CPI and PPI are monthly series.

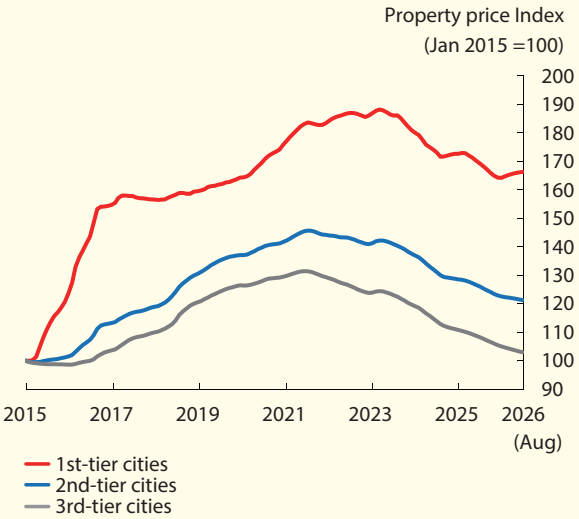
Sources: NBS, Wind and CEIC.

Property and credit markets

The housing market remained soft overall in the first eight months of 2026, though top-tier cities performed relatively better. Housing prices in first-tier cities continued to record positive sequential growth from March to August, recovering tentatively from recent low, while prices in second- and third-tier cities remained soft (Chart 2.8). At the national level, property market activities, including sales, investment, construction and land sales revenue, contracted further (Chart 2.9).

The authorities have maintained a supportive policy stance, emphasising housing market stabilisation. Local governments have rolled out a series of incremental easing measures. New policy measures[7] increasingly focused on urban renewal, affordable housing, "quality homes", property-related services, the relaxation of restrictions, refinements to the housing provident fund system and a shift from pre-sale to completed property sales. This reflects the property sector's ongoing transition towards improving housing quality and people's living standards, alongside its recognised role in supporting households and the broader economy. Overall, policy support remains incremental and city specific.

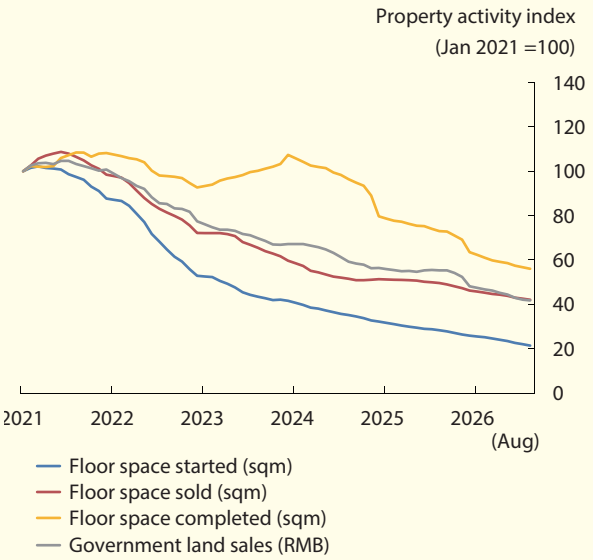
Chart 2.8
Chinese Mainland: Residential property prices by tier of cities



Sources: CEIC and HKMA staff estimates.

[7] Specific measures included the release of the Urban Renewal Plan for the 15th FYP period and related investment plans, a revised regulation on Housing Provident Fund management, and calls for stronger support for housing-related consumption under the broader consumption expansion plan for the 15th FYP period. In addition, top-tier cities such as Beijing, Shanghai, Shenzhen and Guangzhou further relaxed their home purchase restrictions. On 22 May 2026, the State Council issued guidelines to provide basic public services based on habitual residence rather than household registration, in support of the people-centred new urbanisation.

Chart 2.9
Chinese Mainland: Property market activities



Note: The property activity indices are calculated as 12-month rolling sums.
Sources: CEIC and HKMA staff calculations.

In the near term, the housing market outlook remains challenging amid soft economic growth momentum and weak domestic demand. While top-tier cities show signs of stabilisation, lower-tier cities continue to face downward pressures. The nature of current challenges seems to differ from previous years. First, the demand-supply imbalance is no longer driven primarily by oversupply, but by weak household confidence and falling housing demand. Second, while the direct drag from the housing market correction has weakened as the sector's share of the economy has diminished, the indirect impact has become more significant. This includes the pressure on local governments' fiscal conditions and households' balance sheets.

Credit growth remained moderate in the first eight months of 2026, partly reflecting continued weakness in private-sector credit demand. Growth in both outstanding loans and aggregate financing hovered at historically low levels. However, overall risk in the banking sector remained largely contained, with non-performing loan ratios staying low. At the June 2026 Lujiazui Forum, the PBoC fine-tuned interest rate-based operations by specifying a narrower, symmetric interest rate corridor for ad hoc overnight repo and reverse repo rates, and further de-emphasised quantitative indicators.

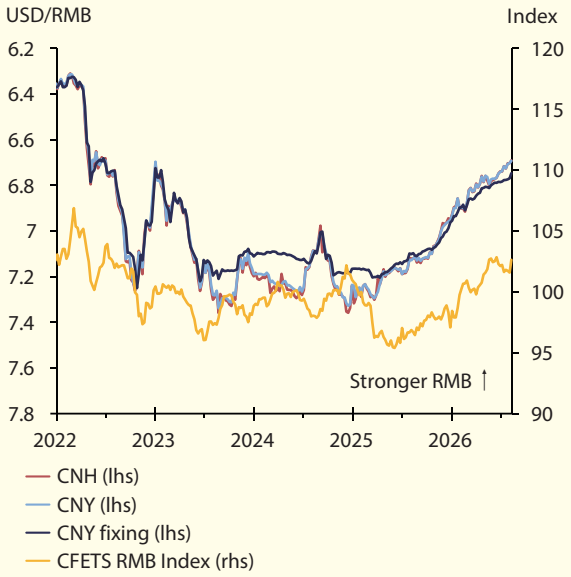
Exchange rate and fund flows

Both the official fixing and market renminbi (RMB) exchange rates strengthened further during the review period, with the onshore market rate firming beyond 6.7 per USD in mid-September (Chart 2.10). Concurrently, the RMB appreciated against the currency basket and outperformed most regional peers, with the China Foreign Exchange Trade System (CFETS) RMB Index reaching a four-year high. This appreciation largely reflected the Chinese Mainland's export competitiveness, the ongoing internationalisation of the RMB, and the resilience of the domestic economy to external shocks. The PBoC signalled a preference for flexible, two-way exchange rate movements and reiterated its commitment to keeping the RMB basically stable. In addition, the PBoC introduced fresh measures to promote RMB internationalisation.[8]

Regarding cross-border bond flows, the onshore Mainland bond market recorded moderate net inflows under various schemes in the first seven months of 2026. However, outstanding foreign holdings of Mainland bonds in the interbank market continued to decline, albeit at a slower pace (Table 2.A). In June 2026, the authorities rolled out new measures to facilitate compliant cross-border capital flows, including an increase in the Qualified Domestic Institutional Investor (QDII) quota, following strengthened enforcement against illegal cross-border stock trading in May.

[8] On 17 June 2026, the PBoC announced a new set of initiatives at the 2026 Lujiazui Forum to further advance RMB internationalisation, including (i) the launch of the Foreign and International Monetary Authorities RMB Repurchase Facility, which provides RMB liquidity to overseas central bank-type institutions against high-grade Chinese bonds as collateral, and (ii) approval for six major domestic banks to conduct offshore RMB transactions in the Shanghai Free Trade Zone. On 7 July, the PBoC announced (i) an increase in the annual quota for Southbound Bond Connect to RMB 800 billion and (ii) an expansion of the HKMA's RMB Business Facility to RMB 500 billion.

Chart 2.10
Chinese Mainland: Onshore and offshore renminbi exchange rates and CFETS RMB Index



Note: "CNY" and "CNH" refer to onshore and offshore renminbi exchange rates respectively.

Sources: Bloomberg and HKMA staff estimates.

Table 2.A
Chinese Mainland: Cross-border bond flow indicators

(RMB bn)	2025	H1 2026	Mar 26	Apr 26	May 26	Jun 26	Jul 26
Northbound Bond Connect	233	139	26	46	41	28	23
CIBM Direct and QFI	1,051	543	89	94	117	116	135
Change in foreign holdings in the interbank market	–698	–264	–134	–67	87	–13	11

Notes: Bond flows are measured by net buying flows for the Northbound Bond Connect and the China Interbank Bond Market Direct Scheme (CIBM Direct) and Qualified Foreign Investor Scheme (QFI).

Sources: Wind, CFETS and HKMA staff estimates.

Box 1
Chinese Mainland's merchandise trade in artificial intelligence-related products

How to classify A.I.-related trade?

After a resilient 2025 amid the China-US trade tensions, merchandise trade growth in the Chinese Mainland unexpectedly accelerated in 2026. From January to August 2026, nominal exports (in USD terms) surged by 19.3% year on year, while imports rose even more sharply by 27.0%. The A.I. boom was widely cited as the primary driver behind this trade surge.

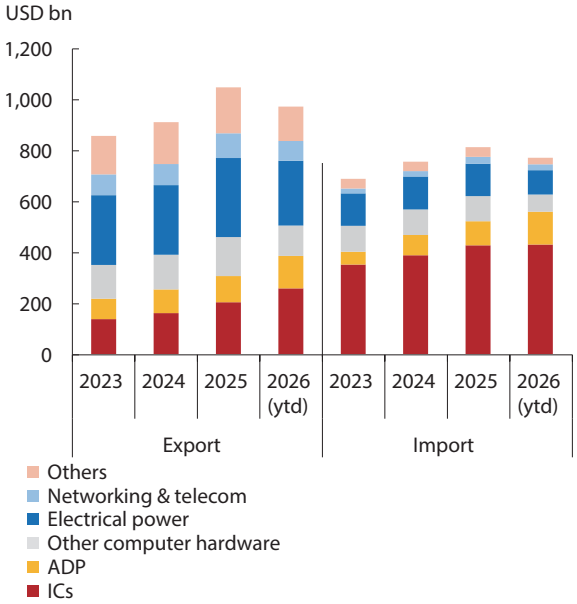
We utilise a recent research paper[9] that employs a large language model (LLM) classification tool to map product codes in US trade data to A.I.-related goods. To ensure comparability, we consolidate the paper's A.I.-related Harmonized System (HS) 10-digit codes into HS six-digit codes to classify trade from the Chinese Mainland.[10] Given the coarser granularity of HS six-digit codes, our classification may include some non-A.I. goods, meaning that our estimates should be interpreted as an upper-bound approximation of the economy's A.I.-related trade.

Compared to the World Trade Organization (WTO) or market analysts, this framework captures a wider range of goods essential to A.I. infrastructure development and operation. It comprises seven categories: (1) computer hardware; (2) electrical power; (3) networking and telecom; (4) heating, ventilation, and air conditioning systems; (5) building and structural materials; (6) fire safety and security systems; and (7) specialty materials. Category (1) is widely regarded as the core A.I. product category, and includes two segments: (1a) integrated circuits (ICs), such as memory chips; and (1b) automated data processing (ADP) equipment and components, such as computers and memory modules. Despite some overlaps, products unique to the WTO's definition of "A.I.-enabling goods" focus more on upstream manufacturing, particularly the semiconductor production chain. Some market analysts adopt an even narrower, data-driven approach, focusing solely on A.I. hardware segments (1a) and (1b).

Our analysis on A.I.-related trade

Our estimates suggest that the Chinese Mainland's A.I.-related trade has increased notably over the past one or two years, reaching 33% of exports and 36% of imports by August 2026 (Chart B1.1).[11] For the first eight months of 2026, the above-mentioned category (1) computer hardware, particularly IC products and ADP machines, constituted the most important product category for both exports and imports. Notably, the importance of computer hardware has generally grown over time.

Chart B1.1
A.I.-related exports and imports by product



Notes: Data for 2026 are up to August. Category (1) computer hardware consists of ADP machines, IC products and other computer hardware.
Sources: China Customs and HKMA staff calculation.

[9] See Michael E. Waugh (2026), "Trade in A.I.-related products", NBER Working Paper 35053.

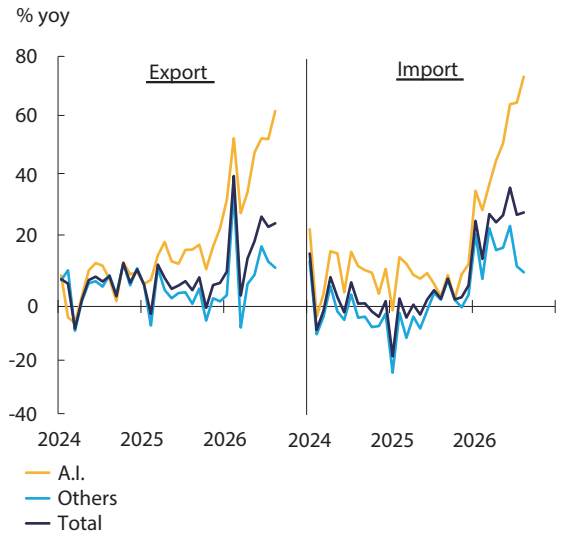
[10] The HS code is a standardised six-digit numerical system which classifies over 5,000 product groups in international trade. Some countries append extra digits for localised data collection or tariff enforcement, so that these extra digits do not refer to the same product.

[11] For comparison, based on the WTO definition of "A.I.-enabling goods", A.I.-related goods are estimated to make up 23% of total exports and 32% of total imports over the same period. Under a narrower definition that includes only IC and ADP products, these goods account for 19% of total exports and 28% of total imports.

Meanwhile, (2) electrical power equipment, such as high-capacity diesel generators for data centres, also played a major role, especially in exports, partly reflecting the Chinese Mainland's entrenched supply chain advantages.[12] Consequently, while the Chinese Mainland runs a trade deficit in core A.I. hardware (Chart B1.1), it records a trade surplus in overall A.I. trade based on a broader classification.

From a broader perspective, A.I.-related trade has been the main driver of total trade growth since early 2026, if not earlier. Year-on-year growth in A.I.-related trade has accelerated sharply since the second half of 2025 (Chart B1.2), fuelled by strong A.I. capital expenditure and the rapid deployment of A.I. models and data centre capacity. A clear divergence has emerged: in terms of trade value, A.I.-related goods are growing much faster than non-A.I. products.

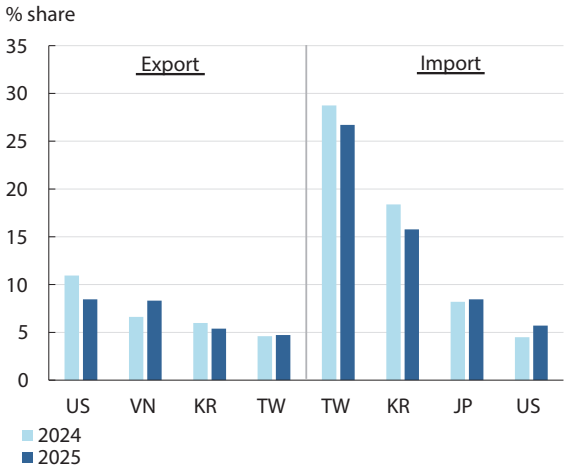
Chart B1.2
Growth in exports and imports by product



Note: Data for 2026 are up to August.
Sources: China Customs and HKMA staff calculation.

By destination, key trading partners include the US, South Korea and Taiwan, while the export markets are relatively more diversified than the import markets (Chart B1.3). Within A.I.-related trade, memory chips and modules have emerged as a standout segment, driven by a global A.I. supply chain centred on a few tech-savvy economies.[13] For instance, the Chinese Mainland imports high-end memory chips from South Korea, performs packaging, testing, and assembly, and then either re-exports the resulting memory modules to South Korea or integrates them into servers for export to the US.[14]

Chart B1.3
A.I.-related trade by major destinations



Note: VN stands for Vietnam; KR for South Korea; TW for Taiwan; and JP for Japan.
Sources: China Customs and HKMA staff calculation.

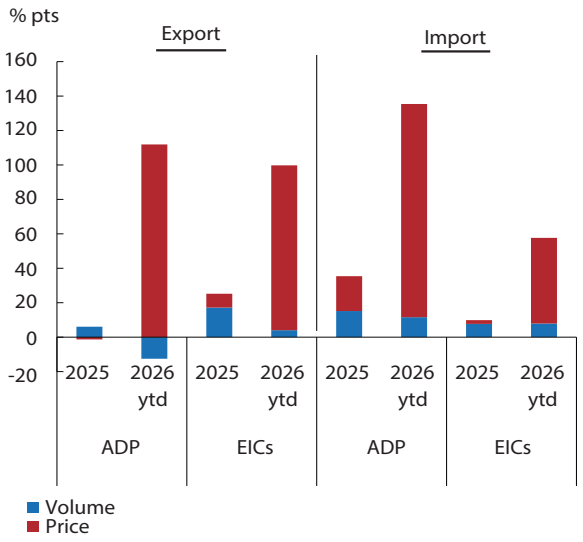
[12] According to news media, import demand from Germany and Southeast Asia has increased recently.

[13] For example, the US, South Korea, the Chinese Mainland, and Taiwan.

[14] The rapid development of A.I. on the Chinese Mainland, driven by initiatives such as the "A.I. plus", has helped drive investment demand, thereby boosting import growth. Amid the global A.I. boom and strong demand, top chipmakers chose to focus on high-end chips, which are more profitable, leaving the market (e.g. mature chips) to Mainland chipmakers. The Chinese Mainland is also an emerging innovator in the semiconductor industry, with a massive chip market.

Market data indicate that, despite variations in specifications and price ranges, memory prices have generally risen by more than 100% since the second half of 2025, driven by strong demand and tight supply. To assess the impact of unit price on trade value, and in the absence of more granular official data, we use China Customs' product categories — (i) electronic IC and (ii) ADP products — as proxies for trade in memory chips and modules. Our analysis shows that the outperformance in memory trade is primarily driven by price increases, especially from 2026 onward (Charts B1.4).[15]

Chart B1.4
Export and import value decomposition for selected A.I. products



Notes: Data for 2026 are up to August. EIC refers to electronic integrated circuit. The y-axis refers to the contribution to year-on-year growth in trade value.
Sources: China Customs and HKMA staff calculation.

The trade outlook and other implications

Looking ahead, A.I.-related products will likely continue to drive the Chinese Mainland's trade growth, with the sustainability of the A.I. boom, memory prices, and A.I. trade relations between China and the US serving as key swing factors. Fundamentally, the Chinese Mainland's strength lies in orchestrating A.I. supply chains and manufacturing certain A.I.-related products, such as data centre power systems,[16] while increasingly focusing on A.I. innovation and technological self-reliance.

The implications for real economic growth warrant close monitoring, as A.I.-related trade has been price led rather than volume driven. The surge in imports does not appear to be driven by a broad-based recovery in domestic demand. Indeed, despite faster growth in merchandise trade value this year, the contribution of net exports to real GDP growth has moderated compared to the previous year.

Furthermore, we are mindful of the "K-shaped" developments associated with A.I.-related trade, where trade benefits concentrate among the "haves", including core A.I. product suppliers, high-tech firms, A.I. talent, and tech-savvy cities both domestically and globally. By contrast, the "have-nots" may fall behind, potentially exacerbating inequality and restricting the positive spillover effects on broader consumption, income, and employment. To address these issues, policymakers may need to implement targeted fiscal and monetary measures and play a stronger role as both an enabler and a redistributor.

[15] This is different from the Chinese Mainland's export resilience in 2024 and 2025, when volume increase was the primary driver and the price effect was generally small or negative.

[16] Some also mentioned the Chinese Mainland's strength in printed circuit boards and optical interconnects.

3. Domestic economy

3.1 *Real activities*

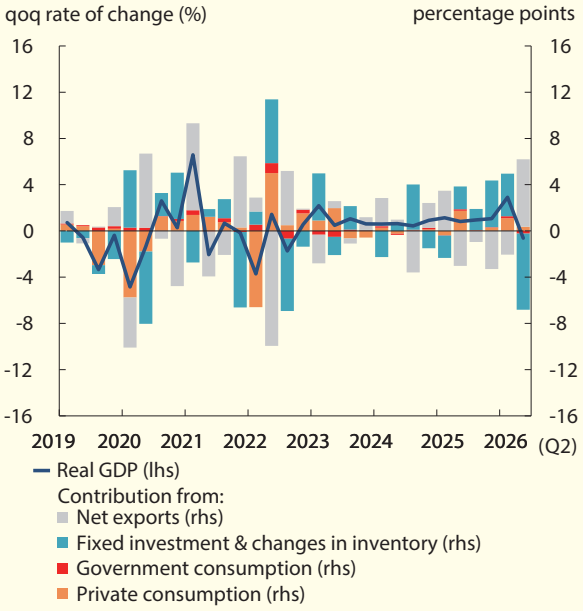
The Hong Kong economy expanded robustly in the first half of 2026, with real GDP increasing by 5.9% and 4.3% year on year in the first and second quarters, respectively (Table 3.A). On a seasonally adjusted quarter-to-quarter basis, real GDP rose notably by 2.9% in the first quarter but fell modestly by 0.6% in the second quarter (Chart 3.1).

Table 3.A
Real GDP growth

		Year-on-year growth rate (%)	Seasonally adjusted quarter-on-quarter growth rate (%)
2025	Q1	+3.2	+1.1
	Q2	+3.3	+0.8
	Q3	+3.8	+0.9
	Q4	+4.0	+1.1
2026	Q1	+5.9	+2.9
	Q2	+4.3	–0.6

Source: Census and Statistics Department (C&SD).

Chart 3.1
Real GDP growth and contribution by major expenditure component



Note: Growth rates are seasonally adjusted.
Sources: C&SD and HKMA staff estimates.

During the review period, economic growth was supported by both strong export performance and resilient domestic demand. Externally, goods exports expanded visibly, underpinned by strong global demand for A.I.-related electronic products (Chart 3.2). Exports of services remained buoyant amid sustained growth in inbound tourism[17] and vibrant cross-boundary financial activities. Domestically, private consumption strengthened further, bolstered by solid consumer confidence and stable asset markets. In tandem, investment spending continued to expand in the first half of the year, partly driven by active property transactions and buoyant private sector capital spending.

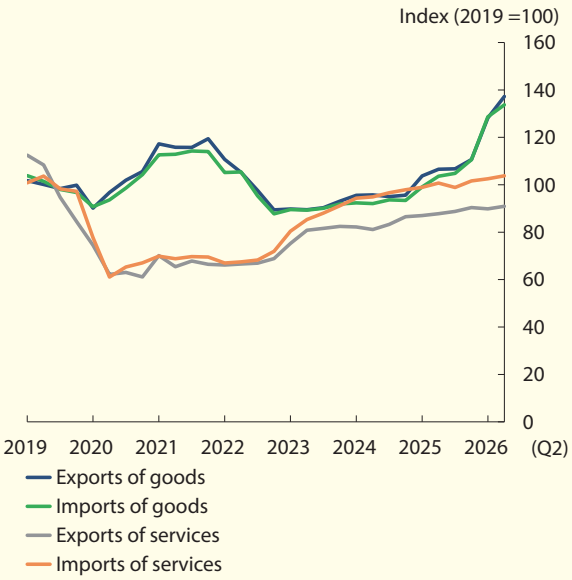
The strong growth suggests that the direct impact of the Middle East conflict on the Hong Kong economy has been limited. This resilience is in part because the actual damage inflicted by the conflict has been less severe than initially feared (see Chapter 2), and in part because the domestic economy possesses inherent structural buffers. Although Hong Kong relies entirely on imports for oil and liquefied natural gas (LNG), the economic shock has been modest. First, the Hong Kong economy is service oriented (accounting for over 90% of GDP) and exhibits low energy intensity.[18] Consequently, energy components constitute only about 3% of the CPI basket, significantly below the APAC range of about 4%–12%. Second, despite high dependence on oil and LNG imports, Hong Kong's exposure to the Strait of Hormuz is relatively low and tends to be indirect, as the bulk (around 80%) of oil imports are from the Chinese Mainland. Finally, policymakers acted swiftly. The

[17] Visitor arrivals into Hong Kong reached about 37 million persons in the first eight months of 2026, representing a 10.5% increase year on year.

[18] According to the International Energy Agency, Hong Kong's energy intensity in 2023 was 1.0 megajoule per unit GDP in constant USD using purchasing power parity, compared to the APAC average of 2.4 megajoules per unit GDP.

Government[19] and the HKMA[20] quickly rolled out targeted measures to mitigate the impact of global energy shock, such as a diesel subsidy and credit relief to affected sectors.

Chart 3.2
Export and import volume



Note: The data are seasonally adjusted.
Source: C&SD.

For the remainder of 2026, the Hong Kong economy is expected to remain resilient and continue its expansion. Externally, robust global demand for A.I.-related products is expected to sustain merchandise export growth. Service exports are anticipated to benefit from rising tourist arrivals, supported by various Government measures to enhance inbound tourism, as well as the steady demand from cross-boundary financial and business activities. Domestically, private consumption is expected to maintain its momentum, supported in part by steady increase in employment earnings, while private investment is likely to remain solid alongside ongoing growth in expenditure on machinery, equipment and intellectual property products.

Taking into account the latest economic situation, the Government revised its real GDP growth forecast for 2026 upward to 3.5%–4.5% from the previous 2.5%–3.5%.[21] Nevertheless, this economic outlook remains subject to various risks and uncertainties discussed in previous chapters. Specifically, the Middle East conflict continues to unfold with significant unpredictability. While current impacts are limited, a prolonged conflict could turn disruptive, leading to higher-for-longer international oil prices, disrupting the global supply chain and trade, and by extension weighing on the Hong Kong economy. Other downside risks include uncertainties surrounding the sustainability of the A.I. investment boom, the trade protectionist policies among major advanced economies, and the US policy rate path.

[19] In April 2026, the Government announced short-term measures to address rising fuel prices, including a diesel subsidy for public and commercial vehicles and vessels, a reduction in tunnel tolls for commercial vehicles, support for public transport operators, and closer monitoring of oil price developments.

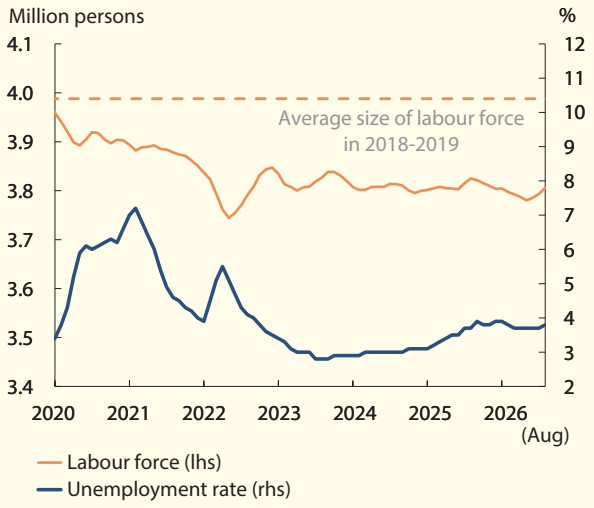
[20] In April 2026, the HKMA and the banking sector launched new support measures to assist local small and medium-sized enterprises (SMEs) in accessing bank financing, strengthening their resilience, and accelerating their upgrade and transformation amid the fast-changing market environment. The 18 banks in the SME Lending Taskforce further expanded their dedicated SME loan funds from HK$370 billion to over HK$450 billion. Additionally, affected sectors such as transport and logistics may receive credit relief, including flexible repayment arrangements, tenor extensions, and more options for trade facilities extensions to alleviate cash flow pressures.

[21] The latest private-sector analysts' consensus forecast for Hong Kong's real GDP growth in 2026 is 4.2%.

3.2 Labour market conditions

The labour market remained broadly stable during the review period, with the unemployment rate at 3.8% in August 2026. The size of the labour force remained below its pre-pandemic level but exhibited an uptick in recent months (Chart 3.3). Looking ahead, labour demand is expected to remain largely stable, although structural shifts in the economy may continue to pose challenges for certain sectors. While prioritising employment opportunities for local workers, the Government will continue to suitably import workers in targeted industries to address manpower shortages and support economic development.

Chart 3.3
Labour market conditions



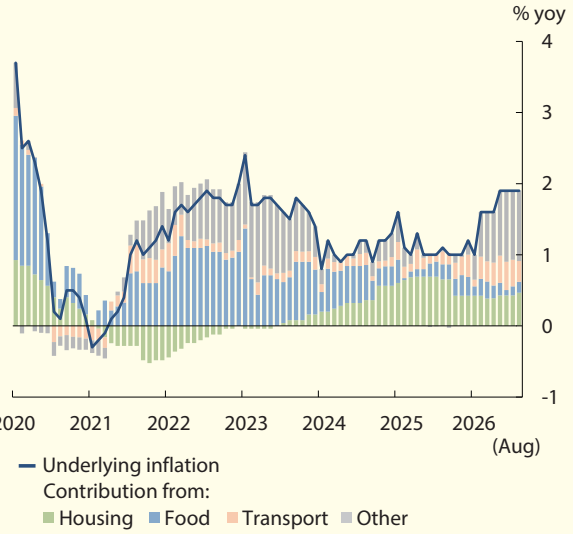
Note: The unemployment rate is seasonally adjusted.
Source: C&SD.

3.3 Inflation

Consumer price inflation increased but remained moderate. On a year-on-year basis, the underlying composite consumer price index rose by 1.4% and 1.8% in the first and second quarters of 2026 respectively, and by 1.9% in August 2026 (Chart 3.4). Fuel-related components picked up in line with higher international oil prices amid the Middle East conflict, while price pressures on food and other components remained largely contained.

Looking ahead, overall inflation is expected to remain manageable. Domestic cost pressures are anticipated to stay mild, thereby mitigating the upward price pressure stemming from the pass-through of the surge in international oil prices to fuel-related components. The Government projects the underlying and headline inflation rates to be 2.5% and 2.6% respectively in 2026.[22]

Chart 3.4
Underlying consumer price inflation and its drivers



Sources: C&SD and HKMA staff estimates.

[22] The market consensus forecast for the headline inflation rate in 2026 is 1.9%.

4. Monetary and financial conditions

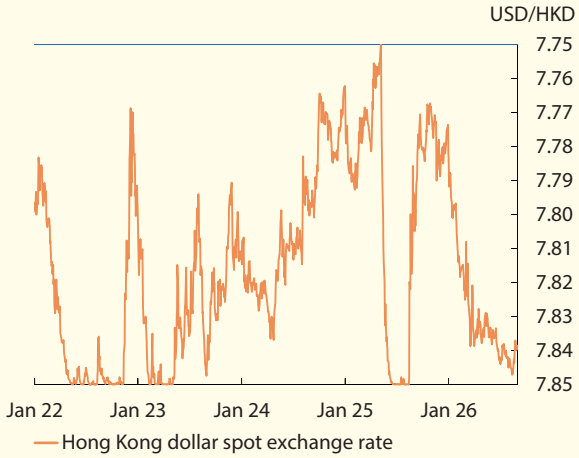
4.1 Exchange rate and capital flows

The Hong Kong dollar (HKD) traded within a range between 7.8080 and 7.8471 during the review period (Chart 4.1). In early March 2026, uncertainty stemming from the Middle East conflict prompted investors to unwind short HKD positions, temporarily driving the HKD stronger. Nonetheless, carry trade activities incentivised by HKD interest rates moving lower than their US dollar (USD) counterparts, subsequently drove the HKD weaker. Market fluctuations were largely driven by flows related to Southbound Stock Connect and other capital market activities.

As the Convertibility Undertakings (CUs) were not triggered during the review period, the Aggregate Balance of the banking system remained largely unchanged at around HK$54.2 billion at the end of August 2026. Day-to-day interbank operations and settlement activities among banks continued to operate in a smooth and orderly manner (Chart 4.2).

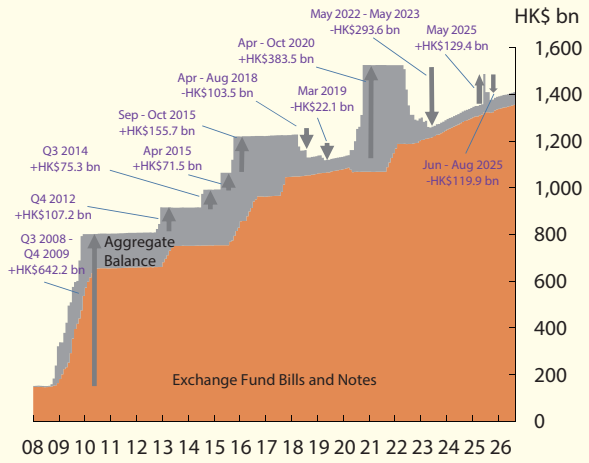
Looking ahead, heightened geopolitical risks, the ongoing military conflict in the Middle East, uncertainty over the US trade policy, and concerns about the sustainability of the A.I. investment boom may increase the volatility of fund flows. However, Hong Kong's ample foreign reserves and resilient financial system position it well to absorb such shocks without compromising financial stability.

Chart 4.1
Hong Kong dollar exchange rate



Source: HKMA.

Chart 4.2
Aggregate Balance and Exchange Fund Bills and Notes (EFBNs)



Source: HKMA

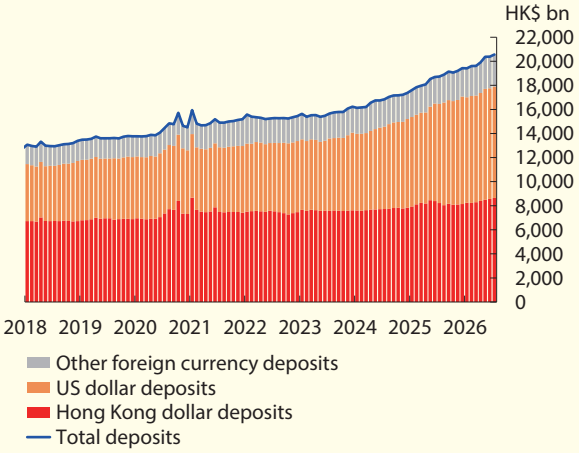
4.2 Monetary environment and interest rates

Hong Kong's monetary environment stayed accommodative during the review period. The HKD Monetary Base remained sizeable and broadly stable at HK$2,080.3 billion as of end-August 2026.

In the first seven months of 2026, total deposits with authorized institutions (AIs) increased by 5.8%. Of this, HKD deposits and foreign currency deposits increased by 6.2% and 5.5% respectively (Chart 4.3). As monetary statistics are subject to volatility from transient factors, such as seasonal funding demand as well as business and investment related activities, it is more appropriate to observe the longer-term trends.

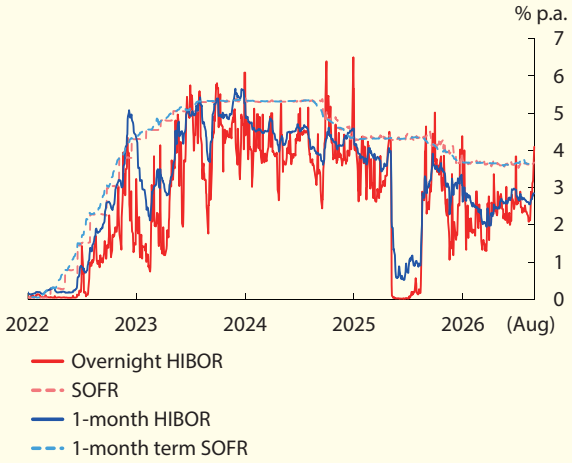
Overall, Hong Kong's interbank market continued to trade in a smooth and orderly manner. In accordance with the expectation and the design of the Linked Exchange Rate System, HKD interbank interest rates generally track their USD counterparts[23] while short-term rates are also influenced by local supply of and demand for HKD funding. Reflecting shifts in seasonal and capital market-related funding demand, short-term Hong Kong Interbank Offered Rates (HIBORs) eased in early March before generally firming thereafter (Chart 4.4).

Chart 4.3
Deposits with authorized institutions (AIs) by currency



Source: HKMA.

Chart 4.4
Hong Kong Interbank Offered Rates (HIBORs) and US dollar Secured Overnight Financing Rates (SOFRs)



Sources: Bloomberg and HKMA.

On the retail front, local banks kept their best lending rates unchanged in the range of 5.00% to 5.50% during the review period, even after the US Federal Reserve's (Fed) rate hike in September 2026. Meanwhile, the average lending rate for new mortgages remained unchanged at 3.26% from January to July 2026. Banks will assess the merit and extent of adjustments for their deposit and lending rates, taking into account factors such as funding supply and demand, prevailing interest rate levels, and their individual funding cost structures.

The HKMA continues to closely engage with banks, reminding them to properly manage liquidity. This includes maintaining close contact with large clients to understand their HKD funding plans, thereby helping banks to plan effectively and avoid hoarding HKD. The HKMA has also advised banks not to be deterred by the perceived "stigma effect" of tapping into its liquidity facilities; banks should feel free to use the HKMA's various liquidity facilities whenever required.

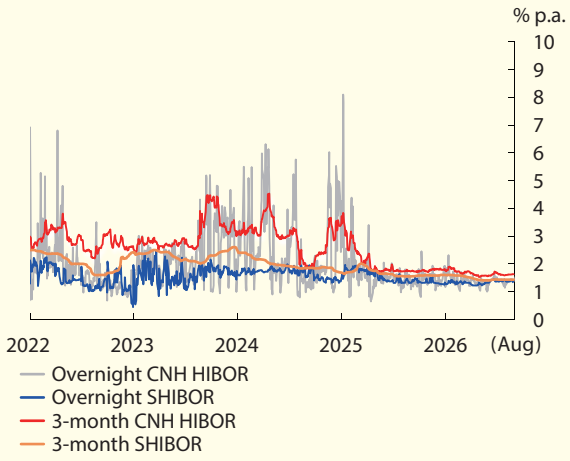
[23] The USD London Interbank Offered Rate (LIBOR) has been discontinued since 1 July 2023 and replaced by the Secured Overnight Financing Rate (SOFR) as its alternative reference rate.

Additionally, improvements in financial infrastructure can enhance the operational efficiency and resilience of the HKD interbank market. Box 2 examines how Fast Interface for New Issuance (FINI) has reduced initial public offering (IPO)-related interbank transfers, dampening the impact of large IPO subscriptions on overnight HIBOR.

Offshore RMB banking business

The offshore renminbi (CNH) interbank market continued to function normally during the review period.[24] The three-month CNH HIBOR has remained below 2% since April 2025. While the overnight CNH HIBOR experienced some fluctuations, it mostly traded below 2% (Chart 4.5). Liquidity conditions in the CNH interbank market remained broadly stable.

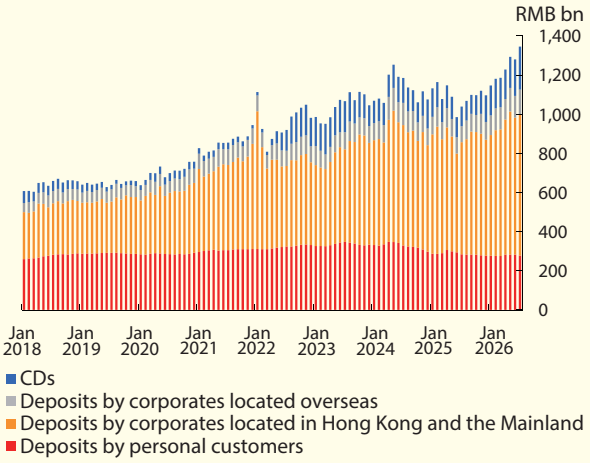
Chart 4.5
Overnight and 3-month offshore renminbi (CNH) HIBOR fixings



Sources: CEIC and Treasury Markets Association.

Hong Kong's CNH liquidity pool expanded during the first seven months of 2026. The total outstanding amount of renminbi (RMB) customer deposits and certificates of deposit (CDs) increased by 22.7% to RMB1,345.2 billion at the end of July 2026 (Chart 4.6 and Table 4.A). Among the total, RMB customer deposits grew by 17.2%, mainly led by corporate customers' deposits. Meanwhile, the outstanding amount of RMB CDs expanded, increasing by 60.8% during the same period.

Chart 4.6
Renminbi customer deposits and certificates of deposit (CDs) in Hong Kong



Source: HKMA.

Table 4.A
Offshore renminbi banking statistics

	Dec 2025	Jul 2026
Renminbi deposits & CDs (RMB bn)	1,096.8	1,345.2
Of which:		
Renminbi deposits (RMB bn)	960.1	1,125.4
Share of renminbi deposits in total deposits (%)	5.5	6.4
Renminbi CDs (RMB bn)	136.7	219.8
Renminbi outstanding loans (RMB bn)	935.0	1,077.8
Number of participating banks in Hong Kong's renminbi clearing platform	210	208
Amount due to overseas banks (RMB bn)	134.5	179.0
Amount due from overseas banks (RMB bn)	134.8	172.8
	Jan - Jul 2026	
Renminbi trade settlement in Hong Kong (RMB bn)	8,178.5	
Of which:		
Inward remittances to Hong Kong (RMB bn)	2,648.0	
Outward remittances to Chinese Mainland (RMB bn)	4,740.1	
Turnover in Hong Kong's RMB Real Time Gross Settlement (RTGS) system (Daily average during the period; RMB bn)	2,471.4	

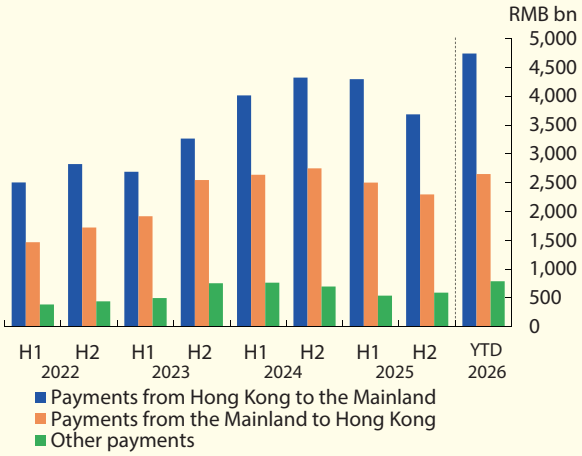
Source: HKMA.

As for other renminbi business, the outstanding aggregate amount of RMB loans expanded by 15.3% in the first seven months of 2026. Renminbi trade settlement handled by banks in Hong Kong amounted to RMB8,178.5 billion in the first seven months of 2026 (Chart 4.7), down by 4.5% compared with RMB8,568.0 billion during the same period in 2025. Nonetheless, the deep RMB liquidity pool in Hong Kong and the

[24] See section 2.3 of Chapter 2 for developments in offshore and onshore renminbi exchange rates.

capabilities and extensive networks of Hong Kong banks continued to support large volumes of RMB payments and financing transactions. During the first seven months of 2026, the average daily turnover of the RMB Real Time Gross Settlement (RTGS) system stayed high at RMB2,471.4 billion, compared with RMB2,759.7 billion recorded in the same period in 2025.

Chart 4.7
Flows of renminbi trade settlement payments



Source HKMA.

Moving forward, the continued development of Hong Kong's CNH ecosystem will further reinforce Hong Kong's role as the leading CNH business hub. To support the wider use of RMB in real economic activities, the size of the HKMA's RMB Business Facility was increased from RMB200 billion to RMB500 billion, and new tenors of 9-month, 2-year and 3-year were introduced in July 2026. The continued upgrading and expansion of the RMB Business Facility aims to provide timely and sufficient RMB liquidity to meet market development needs, assist banks to enhance their RMB business, support the wider use of RMB in the real economy, and radiate offshore RMB funds globally.

The HKMA will explore the introduction of a tendering mechanism of a 7-day offshore RMB liquidity to add a new channel to support banks' short-term RMB funding needs. It will also explore the issuance of offshore RMB short-term debt instruments to support the building of the offshore RMB yield curve, and promote the development of a bilateral currency transaction framework between Indonesian Rupiah and offshore RMB.

In terms of products, continuous efforts to upgrade and expand the family of Connect schemes between the Chinese Mainland and Hong Kong[25] will widen the spectrum of RMB products and tools available for asset allocation as well as liquidity and risk management. This will facilitate greater two-way traffic between the two markets.

As for financial infrastructure, the collaboration between the China Foreign Exchange Trade System (CFETS) and Hong Kong Exchanges and Clearing Limited (HKEX) to develop an electronic fixed income and currency trading platform (the FIC Trading Platform) in Hong Kong will further strengthen the financial cooperation between Hong Kong and the Chinese Mainland. This initiative reinforces Hong Kong's position as an international financial centre and an offshore RMB business hub.[26]

With these developments, Hong Kong will continue to play a unique role in supporting the Mainland's capital account opening, and the Guangdong-Hong Kong-Macao Greater Bay Area cooperation.

[25] The HKMA, the People's Bank of China (PBoC) and the Securities and Futures Commission (SFC) announced a series of new measures to support the development of Hong Kong's fixed income and currency market and offshore RMB business on 7 July 2026. For details, see the press release "New Measures to Support the Development of Hong Kong's Fixed Income and Currency Market and Offshore RMB Business" on 7 July 2026.

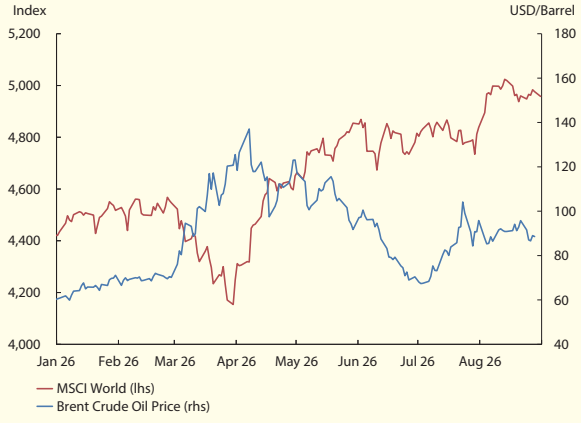
[26] For more details, see the press release "PBOC, HKMA and SFC's joint announcement on developing trading platform in Hong Kong" on 7 July 2026.

Asset markets

4.3 Equity market

Global equity markets experienced significant volatilities during the review period (Chart 4.8). The MSCI World Index fell sharply in March 2026 when the military conflict in the Middle East triggered a surge in oil prices, raising concerns over rising inflationary pressure and a deteriorating global economic outlook. Subsequently, markets rebounded as signs of easing tensions alleviated fears of prolonged energy supply disruptions. This recovery was further supported by strong US corporate earnings and sustained optimism over artificial intelligence (A.I.) developments. Nevertheless, concerns over the sustainability of massive A.I. capital expenditure triggered a sell-off in A.I.-related hardware and infrastructure companies in July 2026, contributing to renewed volatility in global equity markets.

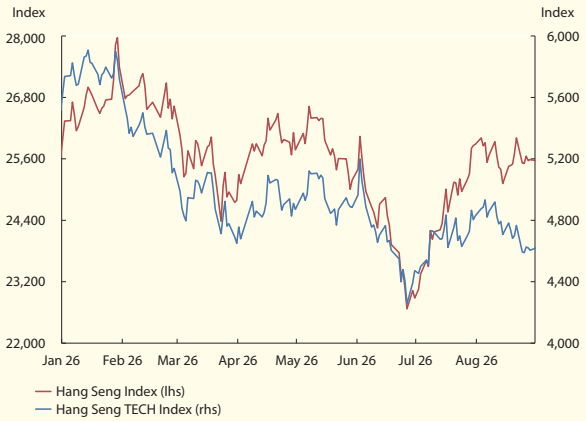
Chart 4.8
MSCI World Index and oil price



Source: Bloomberg and U.S. Energy Information Administration.

In comparison, the Hong Kong equity market recorded weaker performance in the second quarter, reflecting mainly the underperformance of the technology sector,[27] which weighed on market sentiment (Chart 4.9). There was a notable rebound in the local equity market in July, though the divergence in performance remained stark. Overall, the MSCI World Index rose by 9.0% from the end of February to the end of August 2026, while the Hang Seng Index declined by 4.0% during the same period.

Chart 4.9
The Hang Seng Index and Hang Seng TECH Index

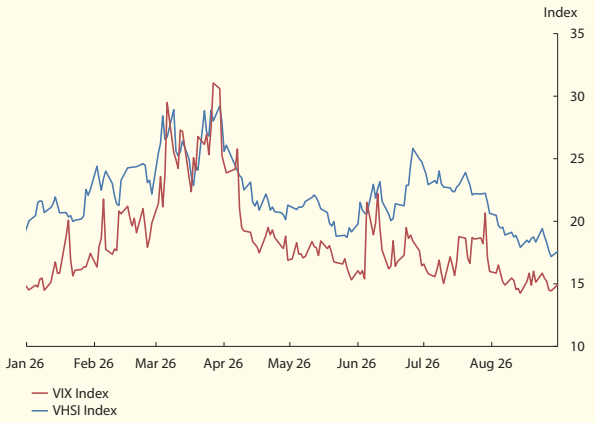


Source: Bloomberg.

Option-implied volatilities for both the S&P 500 and the Hang Seng Indices fluctuated during the review period, driven by heightened uncertainties surrounding the Middle East conflict and the trajectory of A.I. capital expenditure (Chart 4.10).

[27] The Hang Seng TECH Index dropped by 3.8% in the second quarter of 2026. During the same period, the MSCI World Information Technology Index increased by 33.5%. Note that the Hang Seng TECH Index is heavily weighted towards leading Chinese internet platform companies, with a small share of A.I. hardware and semiconductor companies. By contrast, the MSCI World Information Technology Index is dominated by semiconductor, A.I. infrastructure, and hardware companies across developed markets.

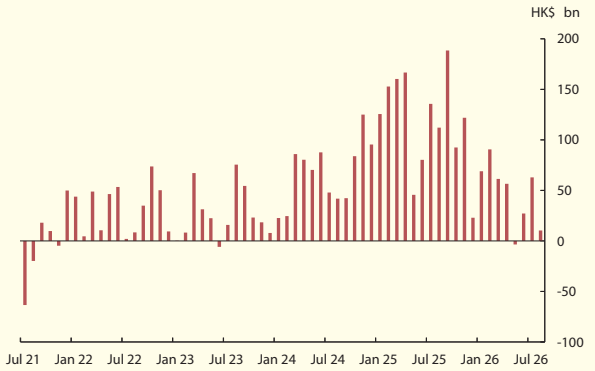
Chart 4.10
Option-implied volatilities of the Hang Seng Index (VHSI Index) and the S&P 500 Index (VIX Index)



Source: Bloomberg.

Inflows into the local equity market through Southbound Stock Connect continued during the review period. Net purchases by Chinese Mainland investors amounted to HK$214.7 billion between the end of February and the end of August 2026 (Chart 4.11).

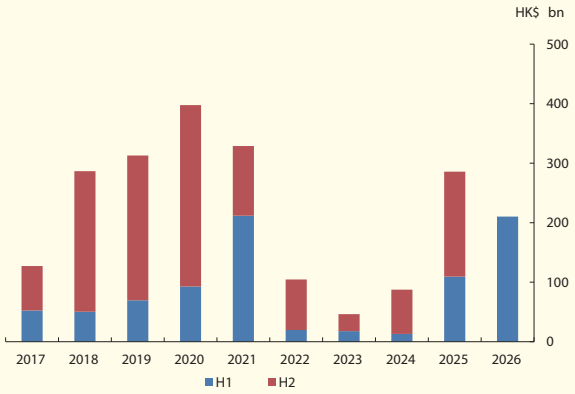
Chart 4.11
Net buying through Southbound Stock Connect



Note: Southbound net buying is the sum of such buying on the Shanghai-Hong Kong Stock Connect and the Shenzhen-Hong Kong Stock Connect.
Sources: CEIC and HKMA staff estimates.

Initial public offering (IPO) activities in Hong Kong remained buoyant. The total funds raised through IPOs in the first half of 2026 reached HK$210.2 billion, increasing by 92.1% from the same period of 2025 (Chart 4.12). This marked the second-highest first half IPO volume to date, supported by a diverse range of companies coming to market.

Chart 4.12
IPO market in Hong Kong



Source: Hong Kong Exchanges and Clearing Limited (HKEX).

Looking ahead, the outlook for global equity markets remains highly uncertain and will depend on several factors.

First, the Middle East conflict remains a key source of risk, as the outcome remains uncertain. Any adverse developments could reignite concerns over global energy supply shocks, clouding the inflation outlook and global economic prospects. This, in turn, could weigh on market sentiment and alter interest rate expectations, thereby putting pressure on global equity markets.

Second, although market sentiment continues to be buoyed by A.I. prospects, it remains unclear whether corporate earnings can justify the high valuations of A.I.-related firms, particularly given their substantial capital expenditure. If revenues fail to meet market expectations, these firms may face the risk of an abrupt price correction, which could trigger broader market volatility. Increasing reliance on debt financing could further amplify such vulnerabilities, especially if financing conditions tighten.

Third, despite recent rate hikes by the US Federal Reserve (Fed) and the European Central Bank (ECB) to combat inflationary pressures, uncertainty over the future interest rate paths remains. This uncertainty is further heightened by the reassessment of monetary policy frameworks by the Fed and the ECB, particularly

the de-emphasis of forward guidance. Greater uncertainty over the interest rate paths may increase volatility in equity valuations.

Fourth, persistent geopolitical and trade tensions could continue to drive a shift in global capital flows as investors seek diversification, potentially amplifying volatility.

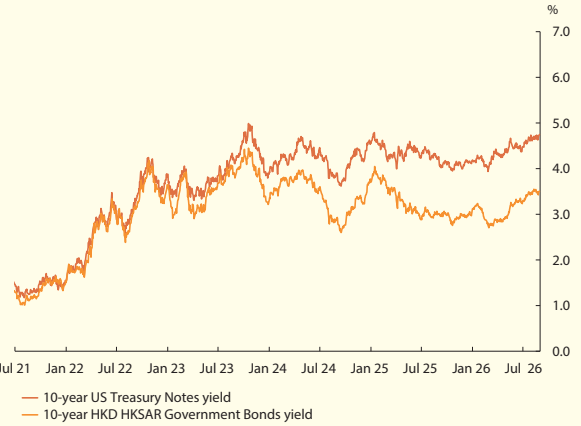
For Hong Kong specifically, market sentiment will also be shaped by the economic growth and technological developments in the Chinese Mainland, given the significant presence of Mainland firms in Hong Kong's equity market.

4.4 Debt market[28]

During the review period, yields on long-term US Treasury Notes increased (Chart 4.13). This increase was driven by rising inflation concerns stemming from oil price volatility amid the military conflicts in the Middle East, alongside upward pressure from risks to long-term US fiscal sustainability due to rising government debt and deficits.

In Hong Kong, the yield on 10-year Hong Kong dollar (HKD) Hong Kong Special Administrative Region (HKSAR) Government Bonds also rose, though it remained well below the yield on 10-year US Treasury Notes. The average yield on HKD corporate bonds also moved up (Chart 4.14). Nevertheless, it was still lower than the yield on USD corporate bonds of similar maturity.

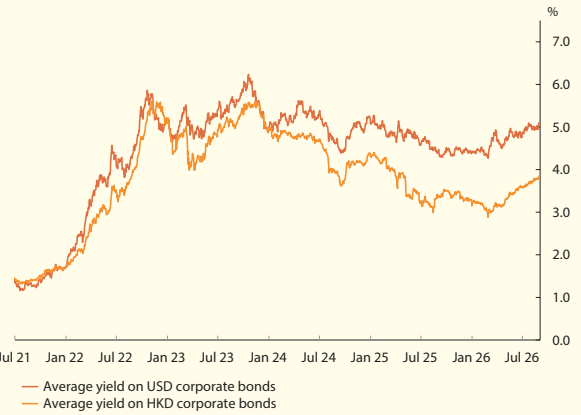
Chart 4.13
Yields on US 10-year Treasury Notes and 10-year HKD HKSAR Government Bonds



Note: Starting from 15 January 2025, the yield on the 10-year HKD HKSAR Government Bonds refers to the yield of the benchmark 10-year HKD bonds issued under the Infrastructure Bond Programme and Government Sustainable Bond Programme. Prior to this date, it refers to the benchmark 10-year HKD bonds issued under the Government Bond Programme.

Sources: Bloomberg and HKMA.

Chart 4.14
Average yields on USD and HKD corporate bonds



Notes: 1. The average yield on HKD corporate bonds is represented by the ICE BofA HKD Local Emerging Market Non-Sovereign Index, which covers HKD bonds issued by corporates and quasi-government entities. 2. The average yield on USD corporate bonds is represented by the ICE BofA 3–5 Year US Broad Market Non-Sovereign Index, which covers USD bonds issued by corporate and quasi-government entities issued in the US with remaining maturities of between 3 and 5 years. 3. The average effective durations of the two indices were 3.6 years and 3.5 years, respectively, as of the end of August 2026.

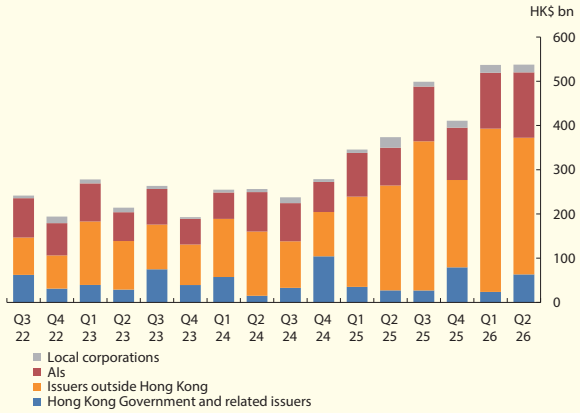
Sources: ICE Data Indices and Bloomberg.

A puzzling development in the global bond market is that the average spread for high-yield (HY) bonds has remained tight, staying below the historical average despite volatile global financial markets. Box 3 explores this phenomenon by linking it to the rapid growth of the private credit (PC) market, and discusses its implications for financial stability.

[28] Debt securities statistics reported in this section include bills, bonds, notes, negotiable certificates of deposit, commercial papers, debentures, asset-backed securities, and similar instruments normally traded in the financial markets that serve as evidence of a debt. Outstanding amounts of debt securities are estimated based on the maturity date of individual debt securities, with early redemptions factored in where sufficient information is available. Estimates may be subject to overestimation. All debt securities figures are subject to revision.

In the first half of 2026, total issuance of HKD-denominated debt securities increased by 11.6% year on year to HK$3,156.9 billion. This growth was driven mainly by non-Exchange Fund Bills and Notes (EFBNs), with issuers outside Hong Kong being the main contributor to the increase. Specifically, issuance of non-EFBN HKD debt securities surged by 49.4% year on year to HK$1,074.6 billion (Chart 4.15).

Chart 4.15
Issuance of non-EFBN HKD debt securities



Notes: 1. Issuers outside Hong Kong include, among others, entities such as multilateral development banks, corporate and government issuers outside Hong Kong. 2. "Hong Kong Government and related issuers" refers to the Government of the HKSAR, statutory bodies and government-owned corporations in Hong Kong.

Source: HKMA staff estimates based on data from Bloomberg, CMU, Dealogic and Reuters.

The outstanding amount of HKD debt securities increased by 22.7% year on year to HK$3,694.1 billion at the end of June 2026 (Chart 4.16), of which the outstanding amount of non-EFBN HKD debt securities rose by 38.7% year on year to HK$2,337.6 billion.

Chart 4.16
Outstanding HKD debt securities by issuer

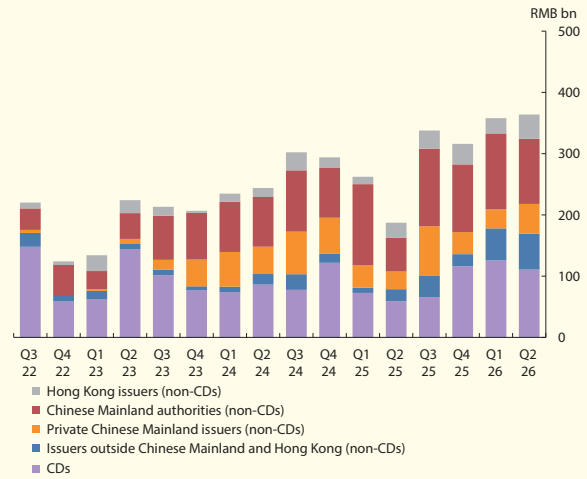


Notes: 1. Issuers outside Hong Kong include, among others, entities such as multilateral development banks, corporate and government issuers outside Hong Kong. 2. "Hong Kong Government and related issuers" refers to the Government of the HKSAR, statutory bodies and government-owned corporations in Hong Kong.

Source: HKMA staff estimates based on data from Bloomberg, CMU, Dealogic and Reuters.

Issuance of offshore Renminbi (CNH) debt securities in Hong Kong rose by 60.5% year on year to renminbi (RMB) 721.9 billion during the first half of 2026 (Chart 4.17), reflecting broad-based growth across issuer groups.

Chart 4.17
Issuance of CNH debt securities in Hong Kong



Source: HKMA staff estimates based on data from Bloomberg, CMU, Dealogic and Reuters.

Looking ahead, the lower HKD interest rate relative to the USD could continue to support activity in the HKD debt market, although the sustainability of this trend depends on the USD interest rate path and HKD fund flows. Over the longer term, continued large-scale issuances in

the public market, combined with investors' demand for greater currency diversification amid persistent geopolitical tensions, could help deepen the HKD debt market and broaden the issuer and investor base.

For CNH debt securities, lower RMB financing costs are expected to persist in the near term, supported by the moderately loose monetary policy in the Chinese Mainland. Meanwhile, policy measures to promote RMB internationalisation, alongside sustained demand for diversification into RMB bonds due to their lower volatility would further support the development of the CNH debt market in Hong Kong.

During the review period, several policy initiatives were introduced to foster the development of Hong Kong's debt market. These initiatives cover green and sustainable finance, technological innovations, and market infrastructure improvement.

On 29 May 2026, the Ministry of Finance of the People's Republic of China (CMOF) completed its inaugural issuance of RMB sovereign green bonds in Hong Kong, totalling RMB6 billion. Warmly received by the market, the issuance enhances the yield curve for Hong Kong's offshore RMB bond market, provides a new investment benchmark for international capital, and attracts more cross-boundary RMB financing and trading activities to Hong Kong.

On 5 June 2026, the HKMA announced that it had convened a Tokenised Bond Expert Group, bringing together industry representatives with relevant experience and interest in Hong Kong's tokenised bond market development. The Group aims to drive further adoption and scalability of tokenised bonds in Hong Kong.

On 11 June 2026, the Hong Kong Mortgage Corporation Limited (HKMC) announced the successful pricing of its inaugural digital bonds, totalling approximately HK$12 billion equivalent, under its US$30 billion Medium Term Note Programme. The issuance marked the largest digital bond issuance globally at the time of issuance, underscoring deep market liquidity and accelerating adoption by institutional investors. In addition, the five-year HKD tranche represented the longest tenor for an HKD-denominated digital bond at the time of issuance, setting a new benchmark in the HKD bond market.

On 29 June 2026, the Financial Services and the Treasury Bureau and the HKMA jointly concluded the first phase of a review regarding the further adoption of distributed ledger technology (DLT) in Hong Kong's fixed income market. Findings in the review suggest that Hong Kong's legal and regulatory environment is already sufficiently flexible for tokenised bond issuances. In the next phase, a legislative review will be carried out to boost the more extensive use of DLT in the fixed income market and digital assets.

On 7 July 2026, the HKMA, the People's Bank of China and the Securities and Futures Commission announced a series of new measures to support the development of Hong Kong's fixed income and currency (FIC) market and offshore RMB business.[29] On the same day, the three institutions jointly welcomed the collaboration between the China Foreign Exchange Trade System (CFETS) and Hong Kong Exchanges and Clearing Limited (HKEX) to develop an electronic FIC trading platform in Hong Kong. This initiative will further strengthen financial cooperation between Hong Kong and the Chinese Mainland, reinforcing Hong Kong's position as an international financial centre and an offshore RMB business hub.

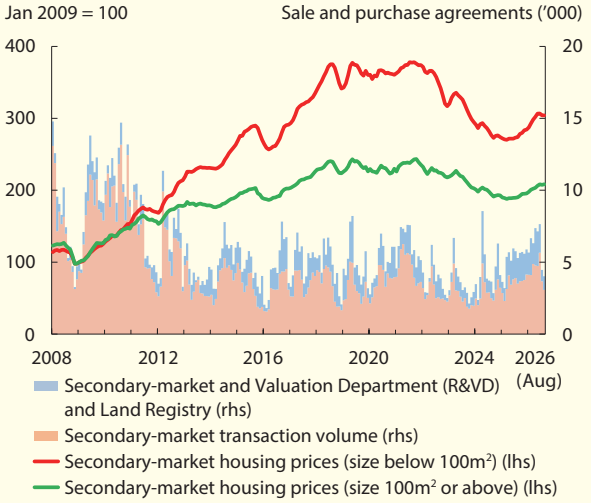
[29] These measures include i) supporting the collaboration of financial infrastructure institutions in Hong Kong and Chinese Mainland to develop a Hong Kong FIC electronic trading platform; ii) further enhancing and expanding the Southbound Bond Connect, iii) supporting the inclusion of onshore bonds issued by the Ministry of Finance and Mainland policy banks that are held under Northbound Bond Connect as eligible margin collateral at the HKFE Clearing Corporation and the SEHK Options Clearing House; iv) enhancing the Northbound Bond Connect operational arrangement, v) further enhancing the Swap Connect; and vi) supporting the launch of 5-Year China Government Bond Futures in Hong Kong. For details, please refer to https://www.hkma.gov.hk/eng/news-and-media/press-releases/2026/07/20260707-3/.

4.5 Property markets

Residential property market

The residential property market was buoyant in the first half of 2026, before stabilising in subsequent months. Supported by vibrant secondary market transactions and the brisk sales recorded in several new project launches by developers, average monthly housing transactions rose notably by 20.4% to 6,802 units in the first half of 2026, compared with 5,648 units in the second half of 2025 (Chart 4.18). Stepping into the third quarter, housing market activities consolidated, with transaction volume decreasing to 4,019 units in August.

Chart 4.18
Residential property prices and transaction volumes



Sources: Rating and Valuation Department (R&VD) and Land Registry.

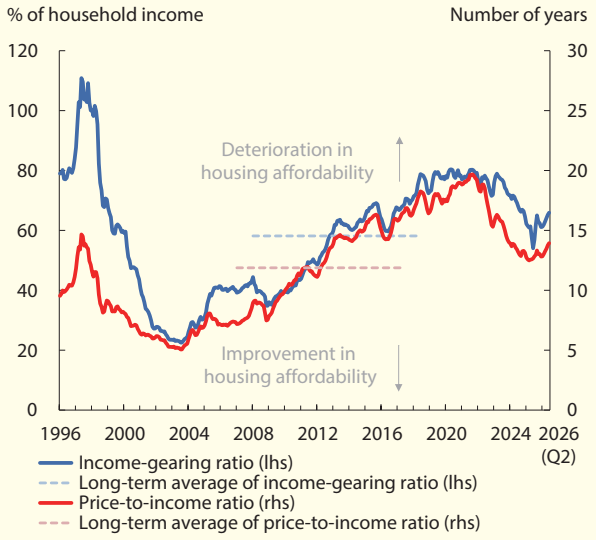
In response to favourable market reception and reduced unsold inventory,[30] developers have gradually reduced discounts on new launches. In tandem, secondary market housing prices accelerated, rising by 7.0% in the first eight months of 2026. Prices of small and medium-sized flats (with a saleable area of less than 100m^2) increased at a slightly faster pace than those for large flats (with a saleable area of 100m^2 or above) (Chart 4.18). More recent market data compiled by property agencies indicated that housing prices remained steady in early September.

In the first half of 2026, housing price growth outpaced household income growth, which reduced housing affordability. Specifically, the housing price-to-income ratio increased slightly from 13.0 years in the first quarter to 13.7 years in the second quarter. Similarly, the income-gearing ratio edged up to 65.1% (Chart 4.19).[31] On the leasing market front, housing rentals continued to increase at a steady pace of 4.9% in the first eight months of 2026, reaching a historical high (Chart 4.20). Residential rental yields remained modest at 3.0% in July.

[30] According to the Housing Bureau, there were around 19,000 unsold units in completed projects as at end-June 2026, compared with 23,000 units at end-December 2025.

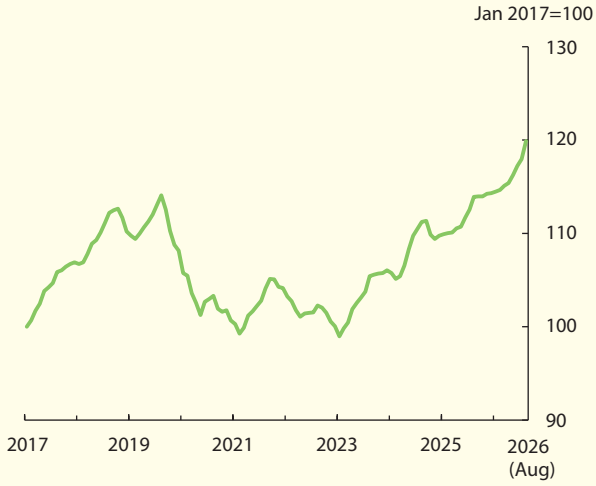
[31] The price-to-income ratio measures the average price of a typical 50m^2 flat relative to the median income of households living in private housing. The income-gearing ratio compares mortgage payment for a typical 50m^2 flat (under a 20-year mortgage scheme with a 70% loan-to-value (LTV) ratio) to the median income of households living in private housing. Note that the income-gearing ratio differs from a borrower's actual debt-servicing ratio (DSR), which is subject to a maximum cap under HKMA prudential measures.

Chart 4.19
Indicators of housing affordability



Sources: R&VD, C&SD and HKMA staff estimates.

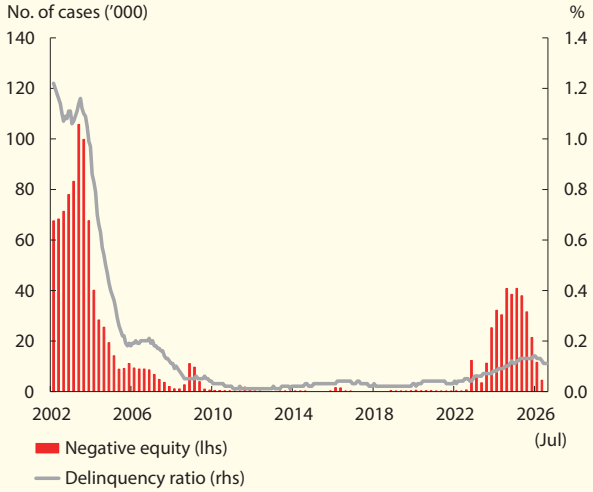
Chart 4.20
Residential property rental index



Source: R&VD.

The rise in housing prices led to a further decrease in the estimated number of residential mortgage loans (RMLs) in negative equity to 4,356 cases at end-June from 11,424 cases at end-March 2026 (Chart 4.21). These cases were mostly related to bank staff housing loans or RMLs under the Mortgage Insurance Programme (MIP), which generally have a higher loan-to-value (LTV) ratio. Meanwhile, the delinquency ratio of all outstanding RMLs eased to a very low level of 0.11% in July 2026,[32] suggesting that the systemic risks relating to banks' RMLs are properly managed on various fronts.

Chart 4.21
Negative equity and mortgage delinquency ratio

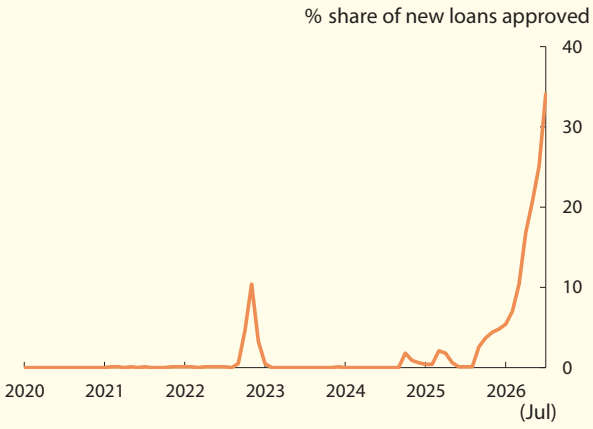


Source: HKMA.

The HKMA continues to monitor market development closely and formulate appropriate supervisory requirements on RMLs to safeguard banking stability. The average LTV ratio and debt-servicing ratio (DSR) for newly approved mortgages remained steady at 61% and 39% respectively in July 2026. On the other hand, reflecting market expectations of future interest rate dynamics, fixed-rate mortgage plans became more appealing to homebuyers as a tool to mitigate the risk of interest rate volatility, with their share increasing notably from 5.4% in January to 34.1% in July (Chart 4.22). The HKMA considers that the Hong Kong banking sector maintains ample buffers to withstand potential challenges stemming from the property market.

[32] The delinquency ratio of RMLs in negative equity increased to 1.25% at the end of June 2026, as the aggregate value of RMLs in negative equity fell at a faster pace than the aggregate value of delinquent RMLs in negative equity.

Chart 4.22
Share of fixed-rate mortgage plans



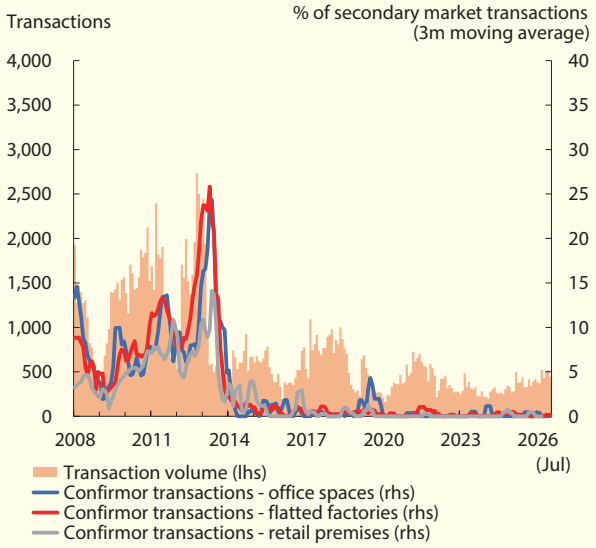
Source: HKMA.

The outlook of the residential property market remains subject to uncertainties, including those surrounding the US interest rate path, that may continue to weigh on housing market sentiment in the near term. On the other hand, the robust domestic economy, combined with the sustained net inflow of talent and overseas students, should continue to support housing demand. Over the longer term, the outlook for the housing market will depend on the supply-demand gap. The Government has identified sufficient land to meet the housing supply target in the next ten years, and will sell land prudently to ensure stable market development.[33]

Commercial real estate market

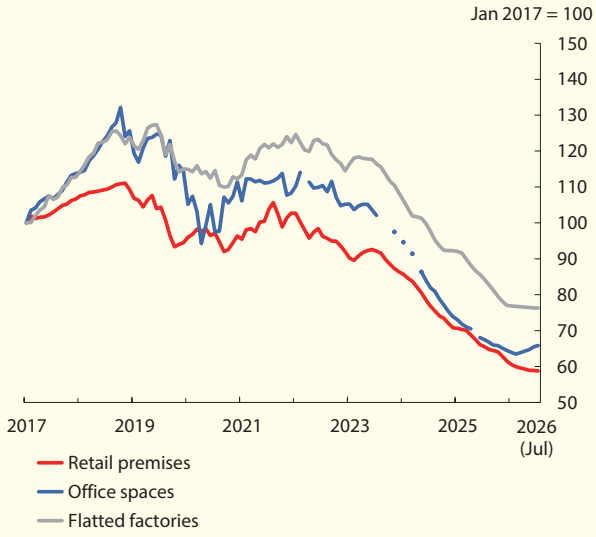
The commercial real estate (CRE)[34] market showed signs of stabilisation alongside improved occupancy rates. The average monthly transaction volume increased further to 455 units in the first seven months of 2026, with speculative activities remaining inactive as indicated by confirmor transactions (Chart 4.23). In tandem, prices of office spaces edged up in recent months, while price declines for retail premises and flatted factories narrowed (Chart 4.24). In the leasing market, office and factory rentals were broadly stable, whereas rentals of retail premises remained soft despite improving business receipts (Chart 4.25). Overall, rental yields across segments edged up to 3.9% – 4.4% in July.

Chart 4.23
Transactions in commercial real estate



Sources: R&VD and Centaline Property Agency Limited.

Chart 4.24
Commercial real estate price indices

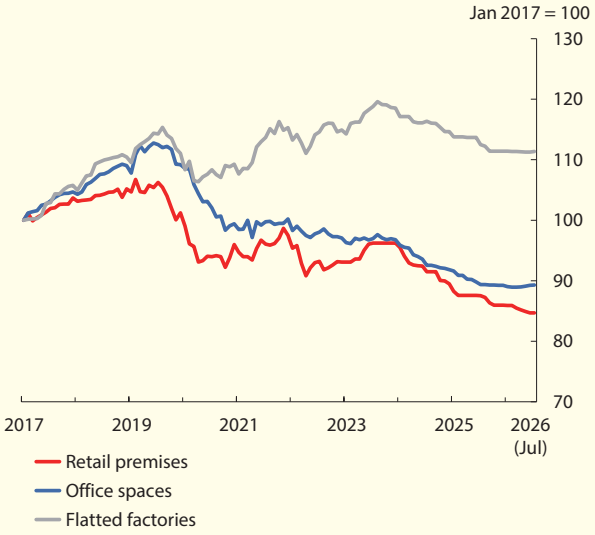


Note: The price index of office spaces could not be compiled in certain months due to insufficient transaction data for analysis.
Source: R&VD.

[33] According to the Long Term Housing Strategy Annual Progress Report 2025, the 10-year total housing supply target from 2026–27 to 2035–36 is 420,000 units, including 294,000 units for public housing and 126,000 units for private housing.

[34] CRE includes office spaces, retail premises and flatted factories.

Chart 4.25
Commercial real estate rental indices



Source: R&VD.

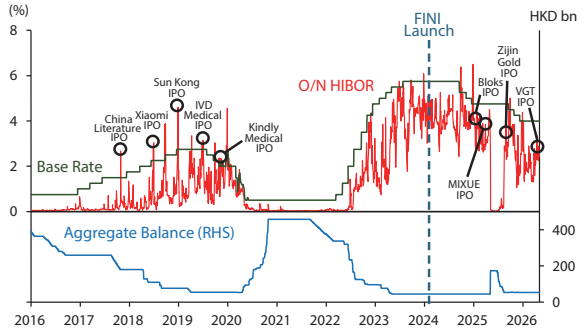
The near-term outlook for the CRE market is uneven. Grade A offices in core districts could see some stabilisation, driven by reviving leasing demand from the finance and insurance sectors, while office vacancy rates in some non-core locations may face ongoing pressure. Meanwhile, the retail segment may continue to face challenges from e-commerce competition and shifting consumption patterns. In response to these conditions, the Government has announced measures to bolster the commercial property market, including the suspension of general commercial land sales in 2026–27.

Box 2
Fast Interface for New Issuance and the Hong Kong Dollar Interbank Market during Initial Public Offerings

Introduction[35]

Large IPOs in Hong Kong have historically generated substantial short-term funding needs and, at times, exerted upward pressure on HKD interbank rates. Under the previous IPO settlement arrangement, banks acting for IPO subscribers (intermediary banks) were required to transfer the full subscription monies to banks collecting funds on behalf of issuers (receiving banks). For heavily oversubscribed IPOs, this process could generate large temporary interbank payment flows, tighten liquidity conditions, and contribute to spikes in the overnight HIBOR, as illustrated in Chart B2.1.

Chart B2.1:
Overnight HIBOR with IPO annotations



Sources: HKMA, HKEX, Bloomberg.

On 22 November 2023, HKEX launched FINI, a modernised digital platform for IPO settlement. FINI was designed to alleviate IPO-related liquidity pressures by reducing interbank transfers and minimising both the amount and duration of funds locked up. Using transaction-level data from the HKD RTGS system, alongside IPO and money market data, this box assesses whether FINI has mitigated the impact of IPO activity on the HKD interbank market.

How FINI changed the IPO settlement process

Before FINI, intermediary banks were required to transfer the full subscription amounts to receiving banks during the subscription period. Unused subscription monies were subsequently returned through another round of interbank transfers after allotment results were finalised. The liquidity implications of such round-trip transfers were particularly pronounced in Hong Kong, where IPOs are often heavily oversubscribed. For large IPOs, these payment flows could be substantial and remain locked up for several business days.

FINI changed the IPO settlement process in three important ways:

- **Reducing interbank transfers:** FINI removed the requirement for full interbank funding at the subscription stage. Under the new system, interbank transfers take place only after allotment results are finalised and are based on the actual allotment amounts. For heavily oversubscribed IPOs, these amounts are often orders of magnitude smaller than the initial subscription totals. This eliminates both the upfront transfer of the full subscription amount and the subsequent round of refund transfers.

- **Reducing the volume of locked-up funds:** Prior to FINI, interbank funding arrangement served to ensure that subscriptions were backed by sufficient funds. FINI introduced an intrabank pre-funding requirement instead. For heavily oversubscribed IPOs, this requirement is met on a compressed basis, significantly reducing the volume of funds locked up relative to the subscribed amount.

[35] For details, see Cheung et al. (2026). "Fast Interface for New Issuance (FINI) and the Hong Kong Dollar Interbank Market During IPOs". HKMA Research Memorandum, 04/2026

- **Shortening the settlement cycle:** By digitalising and streamlining the end-to-end IPO settlement process, FINI shortened the settlement cycle from typically three to six business days to just one business day.

Using daily IPO, RTGS, and money market data from January 2016 to December 2025, we examine whether FINI reduced IPO-related interbank transfers and reserve concentration, and whether it mitigated the impact of IPO subscriptions on interbank rates.

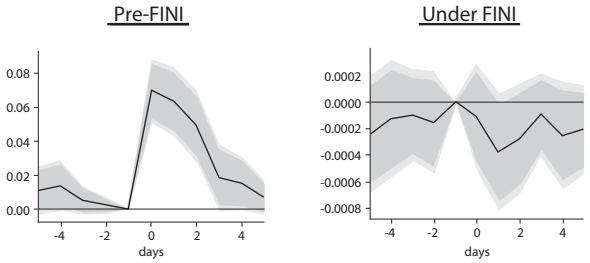
FINI reduced IPO-related interbank transfers

Transaction-level RTGS data reveal that the volume of IPO-related interbank transfers fell by 99.4% compared with the pre-FINI period. This indicates that the new settlement arrangement has largely eliminated the sizeable cross-bank payment flows previously associated with IPO funding and refunds.

The reduction in interbank transfers is also reflected in the distribution of reserve balances across banks. Before FINI, large IPO subscriptions tended to shift reserve balances from intermediary banks to receiving banks, temporarily increasing the concentration of liquidity within the banking system. This concentration could, in turn, tighten funding conditions for banks with liquidity needs.

To quantify this effect, we constructed a daily Herfindahl-Hirschman Index (HHI) of banks' reserve balances and estimated its dynamic response to IPO subscription interest. Subscription interest is scaled by the Aggregate Balance, which serves as a gauge of the funding pressure generated by IPO activity relative to the amount of interbank liquidity available in the banking system. The results show that, before FINI, large IPOs significantly increased reserve balance concentration for several days. By contrast, under FINI, the estimated impact was statistically insignificant (Chart B2.2).

Chart B2.2: Response of reserve balance concentration (HHI) to IPO subscriptions



Note: HHI is measured on a 0–1 scale. Dark and light shaded areas show the 90% and 95% confidence intervals respectively.

Sources: HKMA staff calculations, HKEX website, Bloomberg, HKD RTGS.

FINI mitigated impact of IPOs on overnight HIBOR

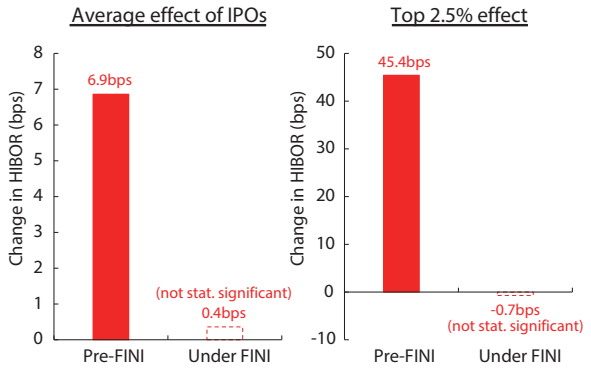
We next use regression analysis to examine whether the reduction in interbank transfers and reserve concentration lessened the impact of IPO subscriptions on overnight HIBOR.

We find that prior to the introduction of FINI, IPO subscriptions had a significant positive effect on overnight HIBOR.[36] On average, an increase in IPO subscription interest equivalent to the Aggregate Balance was associated with a 6.9-basis-point increase in overnight HIBOR, with the effect reaching around 45 basis points in upper-tail scenarios, as captured by the 97.5th percentile of the quantile regression (Chart B2.3).

[36] The regression controls for other factors affecting HIBORs, including the relevant US interest rate, the out-of-the-money USD/HKD risk reversal, changes in the Aggregate Balance, local market conditions, and seasonal funding demand.

This effect diminished substantially after FINI was launched. While the estimated impact of IPO subscriptions on the overnight HIBOR remained positive, it was no longer statistically significant under the FINI regime. This suggests that FINI has been effective in alleviating the short-term liquidity pressures previously associated with IPO funding.[37]

Chart B2.3:
Estimated impact of IPO subscriptions on overnight HIBOR



Note: Estimated effects are scaled to an increase in IPO subscription interest equal to one AB. Solid indicates statistical significance at 10%. Hollow bars are not statistically significant. The top 2.5% effect is quantified using quantile regression at the 97.5th percentile.

Sources: HKMA staff calculations, HKEX website, Bloomberg.

[37] Further analysis shows that only IPOs with subscription interest exceeding the Aggregate Balance had a statistically significant effect. Moreover, IPO-related effects on interbank rates are largely confined to very short maturities. The effect is evident for overnight and, to a lesser extent, one-week HIBOR, but is not statistically significant for one-month or longer tenors. The smaller impact at the one-week tenor is also substantially reduced under FINI, while one-month and longer-tenor HIBORs remain largely unaffected. This suggests that IPO-related liquidity stress is mainly short-lived.

The findings are consistent with a simple conceptual mechanism: for a given level of total reserves, a more uneven distribution of reserve balances can increase interbank market tightness and put upward pressure on overnight interbank rates. By reducing IPO-induced reserve concentration, FINI prevents the temporary scarcity of liquidity among intermediary banks, thereby stabilising overnight HIBOR and easing short-term funding tightness.

Conclusion and implications

In sum, our analysis shows that FINI has materially improved the functioning of the HKD interbank market during IPO periods. The introduction of FINI has sharply reduced IPO-related interbank transfers, mitigated the concentration of reserve balances across banks, and substantially dampened the impact of large IPO subscriptions on overnight HIBOR.

These findings demonstrate how settlement design can limit the spillovers of large financial transactions to money markets. They also suggest that FINI has strengthened Hong Kong's capacity to accommodate large, heavily oversubscribed IPOs without the degree of short-term liquidity volatility observed under the previous arrangement.

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Cheung, J., Luk, P., Yip, R. (2026). Fast Interface for New Issuance (FINI) and the Hong Kong Dollar Interbank Market During IPOs. *HKMA Research Memorandum, 04/2026*.

HKEX (2020). *FINI Concept Paper: Modernising Hong Kong's IPO Settlement Process*.

Keung, C. (2019). Effect of initial public offerings on short-term interbank rates. *Economic Letter No. 2019/12*.

Leung, F. and Ng, P. (2008). Impact of IPO activities on the Hong Kong dollar interbank market. *HKMA Working Paper No. 08/11*.

Box 3
The link between tighter high-yield bond spreads and the shift of weaker borrowers to private credit

Introduction[38]

Yield spread, which refers to the extra yield of a bond relative to a benchmark rate, is an important indicator in the financial market. A puzzling development in the high-yield (HY) bond market is that average spreads have remained tight and below historical averages, despite volatile global financial markets. This box dives into this issue and discusses its implications for financial stability.

Conventionally, tight spreads could be driven by either improved issuer quality or strong investor demand for risk. However, the rapid expansion of the private credit (PC) market offers a plausible alternative explanation. PC has emerged as a vital funding source for firms excluded from traditional bank loans and public bond markets. Furthermore, tailor-made loan terms, greater flexibility, faster execution and lower disclosure requirements also attract corporates to tap funding from PC. Anecdotally, PC has captured a significant share of middle-market lending, particularly among borrowers with weaker financial conditions. As riskier HY bond issuers shift their borrowing to the PC market, the resulting changes in the composition of HY bond issuers could contribute to the tight spreads.

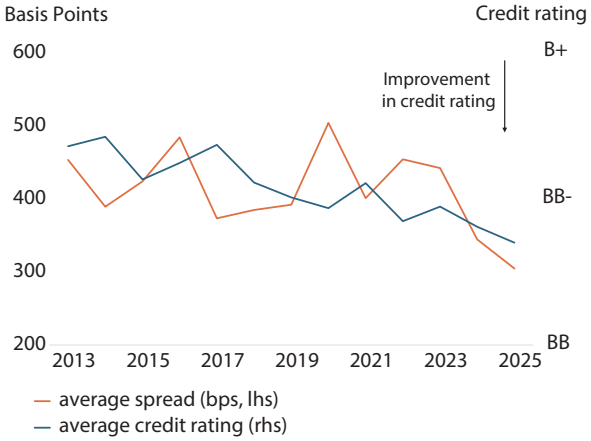
Against this background, this box addresses three questions. First, to what extent are tight HY spreads associated with improvement in the credit quality of issuers? Second, is the improvement linked to the growth of the PC market, and if so, to what extent? Third, is there any sign that firms shifting to PC tend to take higher risk? We assess the final question by examining their leverage. We will also provide implications for financial stability.

[38] For details, see Wu, Lam and Dong (2026): "The link between tighter high-yield bond spreads and the shift of weaker borrowers to private credit", *HKIMR working paper*, forthcoming.

Improved borrower composition and tighter HY bond spreads

Chart B3.1 shows the average spread of HY bonds by year of issuance (the orange line), which has trended down from 454 basis points (bps) in 2013 to 304 bps in 2025. This downward trend is associated with better average credit ratings of these bonds (the blue line).[39] The strong association motivates us to investigate the sources of the improvement in the overall credit quality of HY bond issuances over time.

Chart B3.1:
Average spread of HY bonds and average credit rating of issuers



Note: This figure plots the weighted average credit rating and the weighted average issuance spread of HY bonds issued in each year. Credit ratings are converted into a numerical scale for the calculation of average rating, where 1 corresponds to the highest rating within the HY segment (BB+) and 13 to the lowest reported rating (D). The average numeric rating is then converted back into letter grades for display in the chart. Issuance spread, measured in basis points, represents the yield spread on HY bonds over the relevant benchmark rate.

Source: Dealogic and HKMA staff estimates

[39] The improvement in the credit quality of HY bond issuance is also reflected in the distribution of issuance by rating class. Specifically, in our data sample, the share of BB-rated issuance (the highest rating band in the HY bond market) increased from 57% in 2013 to 71% in 2025. Over the same period, the share of B-rated (the middle rating band) and CCC+ or below (the lowest rating band) issuance declined from 36% to 28% and from 7% to 1%, respectively.

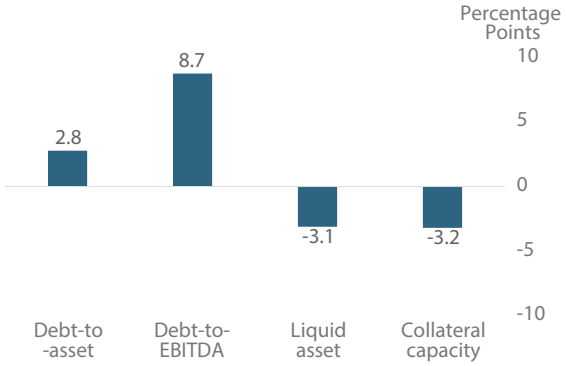
The shift in borrowing by riskier HY bond issuers to the PC market

We hypothesise that riskier HY bond issuers tend to shift to the PC market for funding, altering the composition of the HY bond issuers and driving tighter average spreads. This hypothesis is supported by the fact that average leverage (measured by debt-to-EBITDA) is significantly higher in the PC market than in the HY bond market, making PC particularly attractive to riskier corporates.

To test this, we identify HY bond issuers that also accessed PC ("dual borrowers") from the total sample of HY bonds.[40] We then estimate the probability of PC borrowing using a set of lagged firm characteristics.[41] Specifically, to examine whether riskier HY bond issuers tend to borrow from the PC market, our model incorporates metrics such as leverage (measured by the debt-to-assets or debt-to-EBITDA ratio), liquidity (measured by the liquid asset ratio), and collateral capacity (collateralisable assets[42] to total assets). The estimation controls for other firm-level and sector-level factors.

The results (Chart B3.2) support our hypothesis. In particular, HY bond issuers with higher leverage, lower liquidity, and lower collateral capacity have a statistically higher probability of borrowing from the PC market, all else being equal.[43] We also observe a reduction in HY bond issuances by these firms after they entered the PC market.[44] Taken together, these findings suggest that some riskier HY bond issuers may shift part of their borrowing from the HY bond market to the PC market.

Chart B3.2: Estimated relationship between selected financial metrics and the probability of HY bond issuer borrowing from the PC market



Note: This chart presents the estimated average marginal effects from a logit regression model, measured as the average change in the predicted probability that an HY bond issuer becomes a dual borrower, in percentage points, associated with a one-standard-deviation increase in each financial metric. All estimates are statistically significant at the 10% level.

Source: HKMA staff estimates.

The impact of PC access on risk-taking

We next examine whether HY bond issuers that tap the PC market take on higher risk by examining their leverage. To do so, we compare changes in firms' debt-to-asset ratios before and after their first PC borrowing with changes against similar HY bond issuers that do not borrow from the PC market over the same period.

[40] We identify them using information from Preqin and Capital IQ for firm matching and financial data extraction. After accounting for financial data availability, the estimation sample contains 563 HY bond issuers, of which 91 are classified as dual borrowers. The estimation sample covers the period from 2013 to 2025.

[41] We estimate this using a logit regression model.

[42] Defined as fixed assets and intangible assets excluding goodwill.

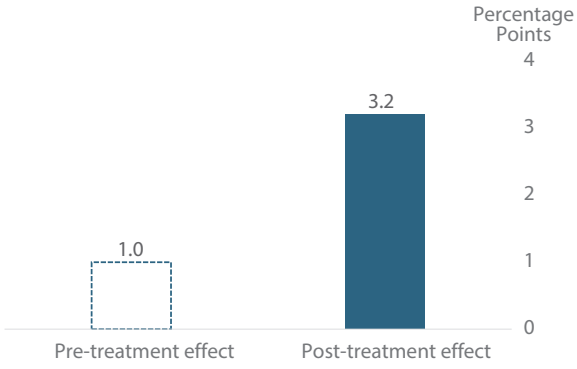
[43] Among the dual borrowers, the share of issuance in the B category and in the CCC+ or below category was 39% and 6%, respectively, compared with 28% and 3% for other HY bond issuers. This further supports the higher riskiness of dual borrowers.

[44] Specifically, the average annual HY bond issuance amount per dual borrower in the sample fell from US$ 633 million before entry into the PC market to US$ 512 million after entry. Dual borrowers' share of total HY bond issuance declined from 35% in 2013 to 24% in 2025.

Specifically, we estimate a staggered difference-in-differences model,[45] where dual borrowers form the treatment group from their first year of PC access onward. In each year, the control group consists of firms that have not accessed PC.[46]

The estimation result (Chart B3.3) indicates that, after accessing PC, dual borrowers' debt-to-asset ratios increased by 3.2 percentage points more than those of other HY bond issuers. This is equivalent to roughly 7.8% of dual borrowers' average debt-to-asset ratio prior to accessing the PC market. The finding suggests that the more accommodative lending conditions in the PC market may have driven some riskier HY bond issuers to tap funding, resulting in higher leverage.

Chart B3.3: Estimated treatment effect of PC entry on firms' debt-to-asset ratio



Note: This chart presents the estimated treatment effect of PC entry on dual borrowers' debt-to-asset ratio (measured in percentage points) relative to HY bond issuers that have not accessed PC, using a staggered difference-in-differences design based on the Callaway and Sant'Anna (2021) estimator. Post-treatment and pre-treatment effects capture the average treatment effect in each year after and before a dual borrower's first observed PC borrowing, respectively. Solid bars indicate estimates are statistically significant at the 10% level.

Source: HKMA staff estimates.

Conclusion

This study has two financial stability implications. Firstly, the average spread of HY bonds is a key conventional indicator for monitoring vulnerabilities of higher-risk corporates. However, the changing composition of HY bond issuers i.e. the shift in borrowing by riskier issuers to the PC market, suggests that this metric should be interpreted with caution. Secondly, our finding that HY bond issuers exhibit higher leverage after entering the opaque PC market underscores the need for enhanced risk monitoring in this sector.[47]

[45] Staggered difference-in-differences applies when units receive treatment at different times. In such settings, the conventional two-way fixed effects estimator may be biased because it can compare newly treated units with already treated ones, and therefore requires a dedicated estimator that addresses this bias. This study employs the estimator proposed by Callaway and Sant'Anna (2021). Details of the Callaway and Sant'Anna (2021) estimator can be referred to Callaway, B. and Sant'Anna, P.H.C. (2021). "Difference-in-Differences with multiple time periods", *Journal of Econometrics*, 225(2), 200-230.

[46] This group includes future "dual borrowers" before they enter the PC market, as well as firms that never access PC.

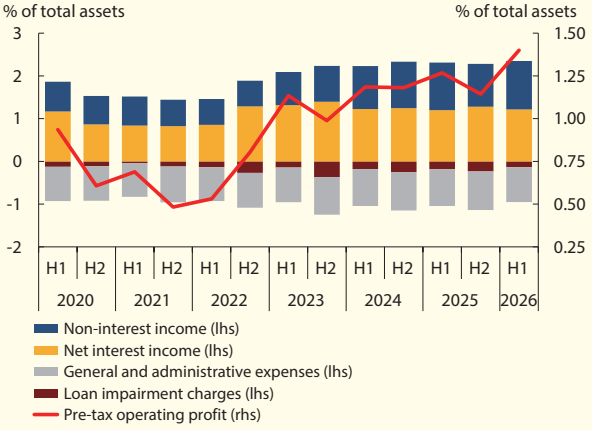
[47] Financial Stability Board (2026). "Report on Vulnerabilities in Private Credit"

5. Banking sector performance

5.1 Profitability

The aggregate pre-tax operating profit of retail banks[48] increased by 20.4% in the first half of 2026, compared with the same period in 2025. This growth was primarily driven by increases in net interest income, fees and commission income, and income from investment held for trading, partially offset by a decrease in income from foreign exchange and derivatives operations. Consequently, banks' return on assets (ROA) improved to 1.40% in the first half of 2026, up from 1.27% in the same period of 2025 (Chart 5.1).

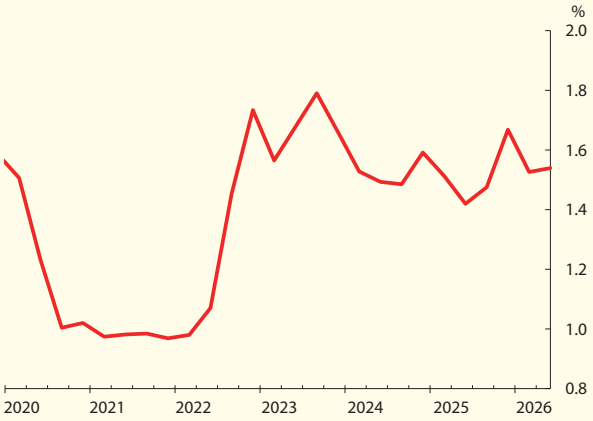
Chart 5.1
Profitability of retail banks



Note: Annualised semi-annual figures.
Source: HKMA.

Meanwhile, the net interest margin (NIM) of retail banks widened to 1.53% in the first half of 2026, compared with 1.47% in the same period of 2025 (Chart 5.2), partly reflecting the increase in Hong Kong dollar (HKD) interest rates during the first half of 2026.

Chart 5.2
Net interest margin of retail banks



Note: Annualised quarterly figures.
Source: HKMA.

The HKD interbank interest rates eased in the first quarter of 2026 as year-end funding demand subsided, before rebounding notably. For instance, the three-month Hong Kong Interbank Offered Rate (HIBOR) decreased by 57 basis points from the end of December 2025 to 2.36% at the end of March 2026, before rising to 2.97% at the end of June 2026. Overall, this represented a net increase of four basis points during the first half of 2026 (blue line in Chart 5.3).

On the retail front, the HKD retail deposit funding costs remained broadly stable during the first half of 2026, as banks kept their HKD savings deposit rates and best lending rates (BLRs) unchanged. Reflecting the developments in both wholesale and retail funding costs, the composite interest rate (a measure of the average cost of HKD funds for retail banks) remained largely unchanged at 1.37% at the end of June 2026 (green line in Chart 5.3).

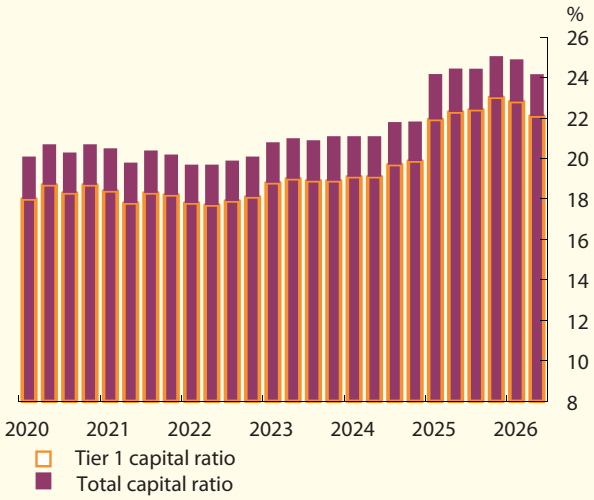
[48] Throughout this chapter, figures for the banking sector relate to Hong Kong offices only, unless otherwise stated.

Chart 5.3
HKD Interest rates



Note: End-of-period figures.
Sources: HKMA and staff estimates.

Chart 5.4
Capital positions of locally incorporated AIs



Note: Consolidated basis.
Source: HKMA.

5.2 *Capital and liquidity positions*

Capitalisation

The Hong Kong banking sector remained well-capitalised. The consolidated total capital ratio of locally incorporated authorized institutions (AIs) stood at a robust 24.2% at the end of June 2026 (Chart 5.4), well above the international minimum requirement of 8%.[49] In addition, the non-risk-based Leverage Ratio of locally incorporated AIs remained healthy at 7.5% at the end of June 2026, exceeding the statutory minimum of 3%.

Liquidity and funding

The liquidity and funding positions of the banking sector, as measured by Basel III liquidity standards, remained sound during the first half of 2026. The average Liquidity Coverage Ratio (LCR) of category 1 institutions and the average Liquidity Maintenance Ratio (LMR) of category 2 institutions were 150.5% and 67.0%, respectively, in the second quarter of 2026 (upper two rows in Table 5A), remaining well above their corresponding statutory minimum requirements of 100% and 25%.[50]

[49] The Tier 1 capital ratio and the Common Equity Tier 1 (CET1) capital ratio were 22.1% and 19.6% respectively.

[50] Under the Banking (Liquidity) Rules, AIs designated as "category 1 institutions" are required to comply with the requirements related to the LCR and Net Stable Funding Ratio. In general, "category 1 institutions" are AIs that either have significant international exposures or are considered systemically important to the local banking sector in light of their size or complexity of business operations. All other AIs are regarded as "category 2 institutions" and are required to comply with the LMR requirement. Among them, AIs designated as "category 2A institutions" must also comply with the local Core Funding Ratio (CFR) requirement. The designation of "category 2A institutions" is based on the institution's business size and liquidity risk profile.

Table 5.A
Liquidity and funding requirement ratios

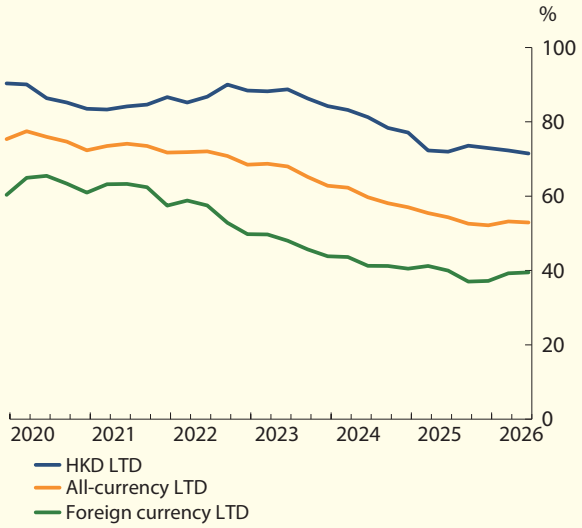
Ratios (%)	Dec-2025	Mar-2026	Jun-2026
Liquidity Coverage Ratio — applicable to category 1 institutions	165.6	160.2	150.5
Liquidity Maintenance Ratio — applicable to category 2 institutions	68.3	66.6	67.0
Net Stable Funding Ratio — applicable to category 1 institutions	141.0	140.9	137.9
Core Funding Ratio — applicable to category 2A institutions	189.0	182.2	184.6

Note: Consolidated basis.
Source: HKMA.

The average Net Stable Funding Ratio of category 1 institutions was 137.9% at the end of June 2026, also well above the statutory minimum of 100%. The average Core Funding Ratio of category 2A institutions stayed at an elevated level of 184.6% (bottom two rows in Table 5A), substantially above the statutory minimum of 75%.

The average all-currency loan-to-deposit (LTD) ratio of all AIs edged up to 52.9% at the end of June 2026, compared to 52.2% at the end of December 2025 (Chart 5.5). The increase was attributable to a rise in foreign currency LTD ratio, partially offset by a slight decrease in the HKD LTD ratio. Specifically, the foreign currency LTD ratio rose to 39.5% at the end of June 2026 from 37.2% at the end of December 2025, while the HKD LTD ratio decreased to 71.5% from 72.9% over the same period.

Chart 5.5
Average loan-to-deposit ratios of all AIs



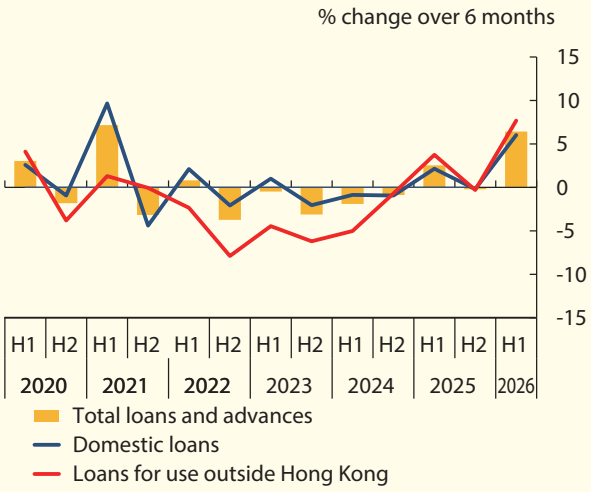
Note: End-of-quarter figures.
Source: HKMA.

5.3 *Credit risk*

Overview

On a half-yearly basis, total loans and advances of all AIs grew by 6.4% in the first half of 2026, reversing a 0.2% contraction in the second half of 2025 (Chart 5.6). This growth was driven by increases in both domestic loans (comprising loans for use in Hong Kong and trade financing), which rose by 6.0%, and loans for use outside Hong Kong, which increased by 7.7% in the first half of 2026.

Chart 5.6
Loan growth



Note: Domestic loans comprise loans for use in Hong Kong and trade financing.
Source: HKMA.

Nonetheless, banks' assessment of near-term credit demand remained cautious. According to the HKMA's Opinion Survey on Credit Condition Outlook, the share of surveyed AIs expecting loan demand to be the same (Table 5.B) increased to 83% in the first half of 2026, up from 71% at the end of 2025. Meanwhile, the share of surveyed AIs expecting higher loan demand dropped from 26% to 10%, likely reflecting heightened uncertainty stemming from the Middle East military conflicts.

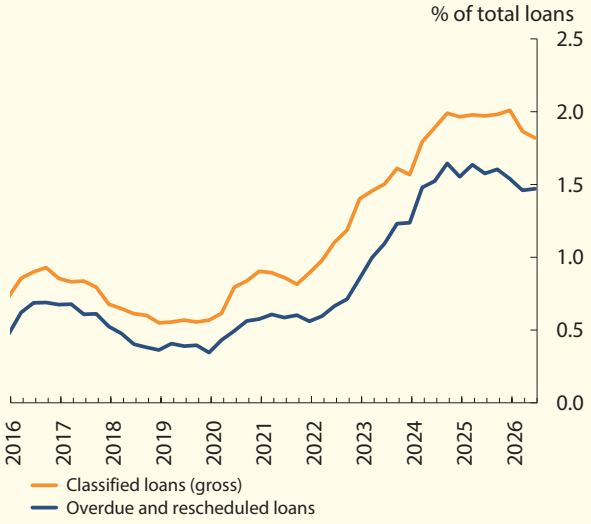
Table 5.B
Expectations of loan demand in the next three months

% of total respondents	Dec-25	Mar-26	Jun-26
Considerably higher	0	0	0
Somewhat higher	26	16	10
Same	71	77	83
Somewhat lower	3	7	7
Considerably lower	0	0	0
Total	100	100	100

Note: Figures may not add up to total due to rounding.
Source: HKMA.

The asset quality of the banking sector remained manageable, with signs of improvement observed in the first half of 2026. The gross classified loan ratio (CLR) of all AIs declined to 1.82% in the second quarter of 2026 from 2.01% at the end of 2025. Meanwhile, the ratio of overdue and rescheduled loans of all AIs decreased mildly from 1.54% at the end of 2025 to 1.47% in the second quarter of 2026 (Chart 5.7).

Chart 5.7
Asset quality of all AIs



Note: Classified loans are those loans graded as "sub-standard", "doubtful" or "loss".
Source: HKMA.

Household exposure[51]

Household debt grew by 5.2% in the first half of 2026, faster than the 2.7% increase in the second half of 2025 (Table 5.C). A breakdown of the data shows that the growth of residential mortgage loans increased to 2.5% in the first half of 2026 amid increased residential property transactions. Concurrently, the growth of personal loans accelerated to 11.8%.

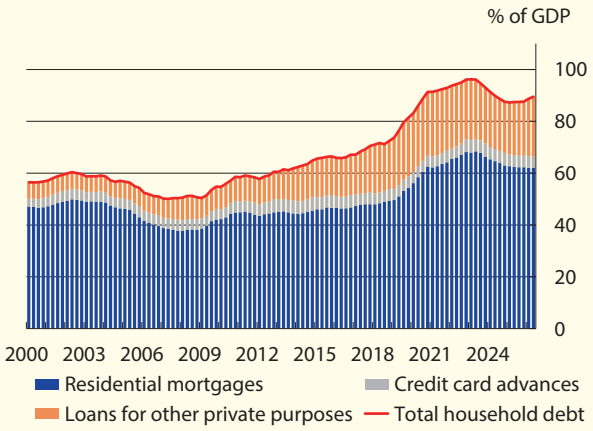
Table 5.C
Half-yearly growth of loans to households by all AIs

	2023		2024		2025		2026
(%)	H1	H2	H1	H2	H1	H2	H1
Residential mortgages	2.6	0.8	0.8	0.6	1.2	2.1	2.5
Personal loans	1.4	–0.3	–1.7	0.5	3.1	4.3	11.8
of which:							
Credit card advances	0.2	10.5	-5.3	6.7	-7.0	9.8	–5.7
Loans for other private purposes	1.6	–2.6	–0.9	–1.0	5.6	3.1	15.8
Total loans to households	2.2	0.5	0.0	0.6	1.8	2.7	5.2

Source: HKMA.

Consequently, the household debt-to-gross domestic product (GDP) ratio rose to 89.5% in the first half of 2026 (Chart 5.8) from 87.6% in the second half of 2025, as household debt expanded at a faster pace than Hong Kong's nominal GDP.

Chart 5.8
Household debt-to-GDP ratio and its components



Notes:
1. Only borrowings from AIs are covered.
2. GDP refers to the annualised GDP, which is the sum of the quarterly GDP in the trailing four quarters.
3. Since December 2018, the figure for household debt has been restated to reflect AIs' reclassification of their working capital loans.

Source: HKMA.

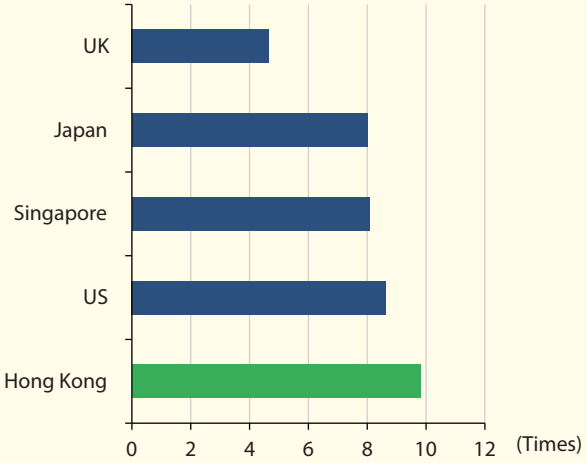
When interpreting the household debt-to-GDP ratio, it is important to note that the denominator of the ratio uses nominal GDP as a proxy for household income to facilitate cross-economy comparison. Therefore, the household debt-to-GDP ratio does not reflect the actual debt servicing burden on households.

A full and objective assessment of the risks associated with household debt requires other factors to be considered. In fact, the average debt servicing ratio (DSR) for new mortgages remained at a healthy 39.4% in July 2026. Furthermore, household net worth remains robust in Hong Kong, with both the net worth-to-liabilities ratio and the safe asset-to-liabilities ratio staying higher than those of other developed economies (Charts 5.9 and 5.10).

[51] Loans to households constitute lending to professional and private individuals, excluding lending for other business purposes. Mortgages account for a major proportion of household loans, while the remainder comprises mainly loans to private banking and wealth management customers secured by financial assets, credit card advances and unsecured personal loans. At the end of June 2026, household lending accounted for 37.9% of domestic lending. In this section, household debt is also referred to as loans to households.

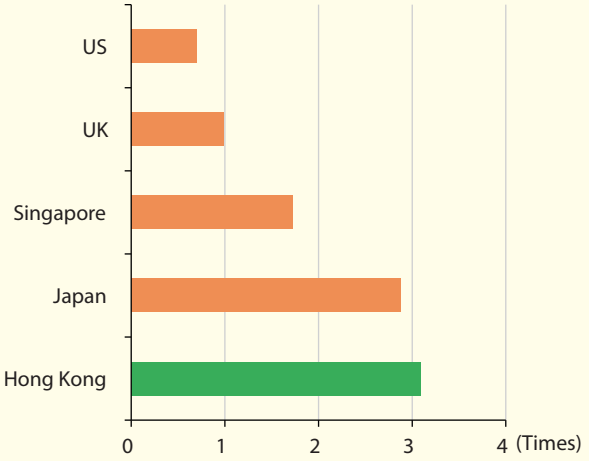
The HKMA continues to closely monitor household indebtedness. The majority of household debts comprises residential mortgage loans, which are governed by the macroprudential policy framework, and collateralised loans to wealth management customers, which are subject to prudent and effective credit risk management measures by banks. In addition, the HKMA requires banks to adopt prudent underwriting standards for credit card advance and unsecured personal loan business. Overall, the HKMA considers the household balance sheet to be healthy and the associated credit risk manageable.

Chart 5.9
Household net worth-to-liabilities ratio for selected economies



Note: Figures for Singapore, the UK and the US refer to end-2025, while figures for other economies (including Hong Kong) refer to end-2024.
Sources: Statistical agencies or central banks of selected economies, and HKMA staff estimates.

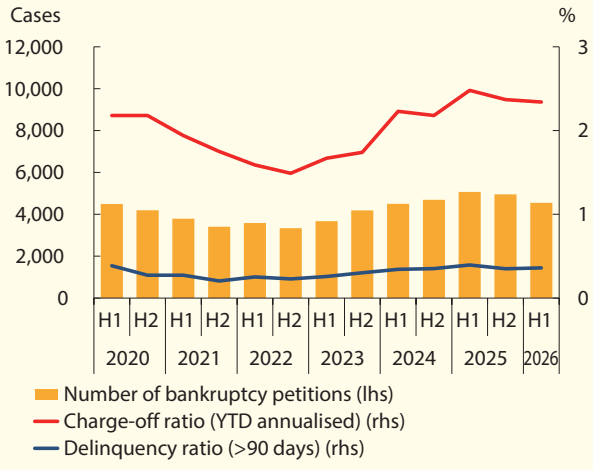
Chart 5.10
Safe assets-to-liabilities ratio for selected economies



Note: Safe assets comprise deposits, as well as currencies if data is available. In the case of Hong Kong, safe assets refer to deposits only. Figures for Singapore, the UK and the US refer to end-2025, while figures for other economies (including Hong Kong) refer to end-2024.
Sources: Statistical agencies or central banks of selected economies, and HKMA staff estimates.

For unsecured household exposure, the associated credit risk remained contained during the first half of 2026. The year-to-date annualised credit card charge-off ratio decreased to 2.34% at the end of June 2026 from 2.37% at the end of 2025 (Chart 5.11). The delinquency ratio was low at 0.36% in June of 2026.

Chart 5.11
Charge-off ratio and delinquency ratio for credit card lending and bankruptcy petitions

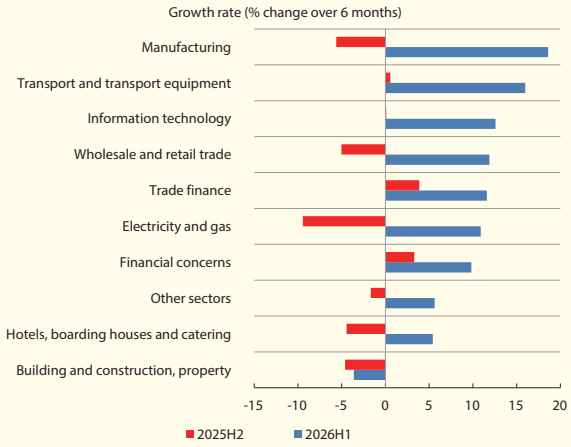


Sources: Official Receiver's Office and HKMA.

Corporate exposure[52]

Domestic corporate loans expanded by 6.5% during the first half of 2026, reversing a modest contraction of 1.9% in the second half of 2025. Lending to most economic sectors recorded positive growth, with particularly strong expansion in the manufacturing, transport and transport equipment, and information technology sectors (Chart 5.12).

Chart 5.12
Growth in domestic corporate loans by selected sectors

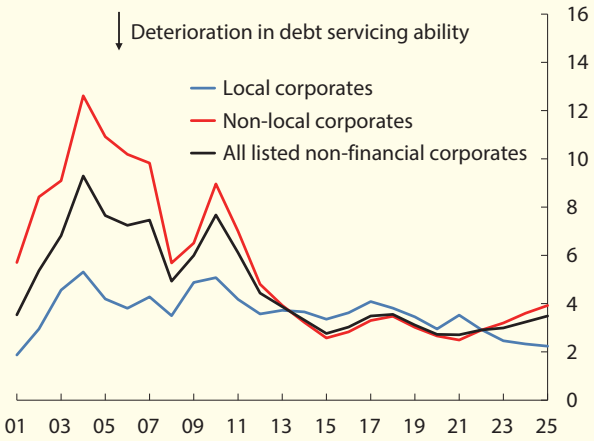


Source: HKMA.

The latest available financial information suggests improving financial health among listed corporates. The debt servicing ability of non-financial corporates listed in Hong Kong, indicated by the weighted average interest coverage ratio (ICR), increased in 2025 (Chart 5.13). Meanwhile, corporate leverage, indicated by the weighted average debt-to-equity ratio, declined moderately (Chart 5.14).

In the longer term, corporate resilience will depend on firms' ability to leverage new technologies to improve efficiency and revenue. Box 4 offers lessons learnt in this regard, drawing on the experience of digitalisation adoption by Hong Kong corporates in recent years.

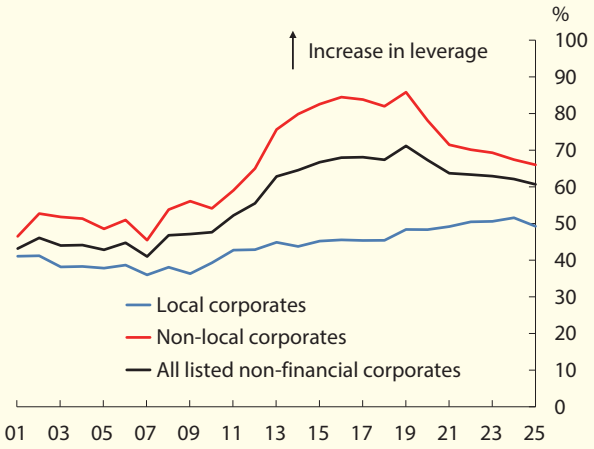
Chart 5.13
Interest coverage ratio of listed non-financial corporates in Hong Kong



Notes:
1. Weighted average figures.
2. The ICR is calculated by dividing the earnings before interest and tax by total interest expenses. A lower value indicates a deterioration in debt servicing ability.
3. All non-financial corporates listed on the Hong Kong Stock Exchange are selected. Local and non-local corporates refer to listed firms that are domiciled in and outside Hong Kong, respectively.
4. Figures are calculated based on information up to mid-August 2026.

Source: HKMA staff estimates based on data from Bloomberg.

Chart 5.14
Leverage ratio of listed non-financial corporates in Hong Kong



Notes:
1. Weighted average figures.
2. The leverage ratio is defined as the ratio of debt to equity. A higher value indicates higher leverage.
3. All non-financial corporates listed on the Hong Kong Stock Exchange are selected. Local and non-local corporates refer to listed firms that are domiciled in and outside Hong Kong, respectively.
4. Figures are calculated based on information up to mid-August 2026.

Source: HKMA staff estimates based on data from Bloomberg.

[52] Excluding interbank exposure. At the end of June 2026, the share of corporate loans in domestic lending was 62%.

Mainland-related lending

The banking sector's total Mainland-related lending increased by 7.6% to HK$4,263 billion (11.5% of total assets) at the end of June 2026 from HK$3,963 billion (11.5% of total assets) at the end of 2025 (Table 5.D). The gross CLR of Mainland-related lending of all AIs[53] further lowered to 1.81% at the end of June 2026 from 1.94% in the fourth quarter of 2025.

Table 5.D
Mainland-related lending

HK$ bn	Dec 2025	Mar 2026	June 2026
Mainland-related loans	3,963	4,133	4,263
Mainland-related loans excluding trade finance	3,733	3,855	3,993
Trade finance	230	278	270

Note. Figures may not add up to the total due to rounding.
Source: HKMA.

Macro stress testing of credit risk[54]

Results from the latest macro stress testing on retail banks' credit exposure suggest that the Hong Kong banking sector remains resilient and capable of withstanding severe macroeconomic and corporate shocks. Table 5.E presents a simulated future credit loss rate of retail banks in the second quarter of 2028 under four specific macroeconomic shocks[55] and one corporate shock, based on information up to the second quarter of 2026. In stressed scenarios, the average expected credit losses two years after different shocks are estimated to be moderate, ranging from 0.86% (interest rate shock) to 1.26% (Hong Kong GDP shock).

Taking into account tail risk, the value-at-risk (VaR) at 99% confidence level (CL) of bank credit loss would increase in all five stressed scenarios, ranging from 2.28% (interest rate shock) to 3.16% (Hong Kong GDP shock).

Table 5.E
The mean and value-at-risk statistics of simulated credit loss distributions[1]

Scenario	Estimated credit loss (% of the loan portfolio) Mean	VaR at 99% CL
Baseline[2]	0.68	1.79
Stressed scenarios[3]		
Hong Kong GDP shock	1.26	3.16
Property price shock	0.87	2.29
Interest rate shock	0.86	2.28
Chinese Mainland GDP shock	1.07	2.65
Corporate Shock	1.21	2.94

Notes:
1. The assessments assume the economic conditions in 2026 Q2 as the current environment. The Monte Carlo simulation method is adopted to generate the credit loss distribution for each scenario.
2. Baseline scenario: no shock throughout the two-year period.
3. Stressed scenarios:
   Hong Kong GDP shock: reductions in Hong Kong's real GDP by 3.2%, 3.6%, 9.3% and 9.4% respectively in each of the four consecutive quarters starting from 2026 Q3.
   Property price shock: Reductions in Hong Kong's real property prices by an average of 12% in each of the four consecutive quarters starting from 2026 Q3.
   Interest rate shock: A rise in real interest rates by 0.1, 0.9, 1.8 and 3.2 percentage points respectively each of the four consecutive quarters starting from 2026 Q3.
   Chinese Mainland GDP shock: An average year-on-year real GDP growth rate of 2% for the four consecutive quarters starting from 2026 Q3.
   Corporate shock: Liquidity and earning shocks on listed corporates in Hong Kong are assumed such that all short-term debts of the corporates could not be rolled over together with a reduction in revenue for the corporates by 50% year-on-year in the first year of the stressed period. The impact of these shocks on the median default probability of corporates is estimated to serve as an input for the stress-testing exercise.

Source: HKMA staff estimates.

53 Figures cover AIs' Hong Kong offices and Mainland branches and subsidiaries.

54 Macro stress testing refers to a range of techniques used to assess the vulnerability of a financial system to "exceptional but plausible" macroeconomic shocks. The credit loss estimates presented in this report are obtained based on a revised framework presented in Box 4 of the *Half-Yearly Monetary and Financial Stability Report* published in September 2023. Estimates in the current report are not strictly comparable to estimates from previous reports.

55 These shocks are calibrated by referencing to the extreme episodes observed in the past. For instance, the Hong Kong GDP shock scenario replicates the severe economic downturn recorded between the third quarter of 2019 and the second quarter of 2020.

5.4 Risks and resilience

As discussed in the previous sections, the Hong Kong banking sector remained resilient. Nevertheless, several downside risk factors, including spillovers from debt vulnerabilities in US A.I. firms, ongoing geopolitical tensions in the Middle East, and uncertainty regarding the future path of US interest rates, could pose challenges to the Hong Kong banking sector going forward.

First, the sharp increase in debt financing of US A.I. firms to support capital expenditures has raised concerns about the debt sustainability of the sector. While fundamentals for large US A.I. firms remain strong, their earnings are pivotal to market sentiment. A substantial downward revision of earnings expectations could trigger a market correction, prompting lenders to tighten exposure to the sector and potentially leading to defaults. Our analysis suggests that any credit stress, should it materialize, would likely be concentrated among smaller A.I. firms in North America, approximately 60% of which are assessed as financially weak based on conventional financial metrics.[56] Although direct credit risk to the Hong Kong banking sector remains contained due to small exposures to A.I. firms in North America,[57] potential spillovers through equity market repricing and broader deterioration in market sentiment warrant close monitoring.

Second, the ongoing conflict in the Middle East remains a key downside risk to global growth outlook. While the direct impact on Hong Kong banking sector should be manageable given its relatively modest cross-border exposures to the region,[58] a prolonged conflict could disrupt global energy supply chains, heighten energy-driven inflationary pressures and weigh on growth outlook, particularly for net oil-importing economies in Asia. Banks with notable exposures to these economies should continue to assess the potential credit risk implications arising from such indirect channels.

Moreover, the future path of US monetary policy rate remains a critical risk factor. While the Fed has raised its US policy rate in September in response to high inflationary pressures, uncertainty remains over the extent and duration of further monetary tightening, which will depend on the evolution of inflation, conditions in the US labour market, and developments in the Middle East conflict. A sharper-than expected rate rise, or a prolonged period of elevated US interest rates, could tighten global financial conditions and push up interest rates in the region. This could weigh on corporate profitability and strain debt-servicing capacity, posing challenges to banks' credit risk management for their corporate exposures.

Nonetheless, given the robust capital and liquidity positions, combined with sufficient provisions, the Hong Kong banking sector is well positioned to withstand shocks arising from these downside risks.

[56] Firms are assessed as financially weak if they have an interest coverage ratio below 1 for two consecutive years, a debt-to-earnings before interest, taxes, depreciation, and amortization (EBITDA) ratio greater than 6, or a debt-to-asset ratio greater than 1.

[57] Based on a representative sample of Hong Kong banks' corporate loans, exposures to A.I. firms in North America account for less than 1% of Hong Kong banks' corporate loans.

[58] The Hong Kong banking sector's external claims on Middle East jurisdictions amounted to HK$924 billion, accounting for 4.7% of total external claims at the end of June 2026.

The countercyclical capital buffer (CCyB) for Hong Kong

The CCyB is part of the internationally agreed Basel III standards, designed to enhance the resilience of the banking sector against system-wide risks. This buffer can be reduced during downturns, allowing banks to continue providing credit to support the real economy. The latest applicable jurisdictional CCyB for Hong Kong, announced on 18 October 2024, is 0.5%.[59]

In setting the CCyB, the Monetary Authority considered a series of indicators (Table 5.F), including an "indicative buffer guide" produced by the Initial Reference Calculator (IRC). The IRC is a metric that provides a guide for the CCyB by combining information from the gap between the ratio of credit-to-GDP and its long-term trend, the gap between the ratio of residential property prices to rentals and its long-term trend, and the Positive Neutral CCyB.[60] The setting of the CCyB for Hong Kong is, however, not a mechanical exercise. The Monetary Authority will consider a broad range of reference indicators ("Comprehensive Reference Indicators") and all relevant information available in addition to the indicative buffer guide produced by the IRC.[61]

Based on the latest assessment using the second quarter data of 2026 and the Positive Neutral CCyB according to the revised IRC formula,[62] the IRC signalled a CCyB of 1%. The projection based on all available data at the decision date suggests that the IRC would likely signal a CCyB of 1% when all relevant data for the third quarter of 2026 become available.

Considering the Comprehension Reference Indicators and all relevant information available at the time of the decision in September 2026, and noting that the two primary indicators remain deep in the negative, the Monetary Authority considered it appropriate to maintain the CCyB at its current level.

[59] For details, see the announcement of the CCyB to AIs in October 2024 (https://www.hkma.gov.hk/eng/key-functions/banking/banking-legislation-policies-and-standards-implementation/countercyclical-capital-buffer-ccyb/).

[60] The Positive Neutral CCyB, currently at 1% in Hong Kong effective from 1 April 2024, is a floor for the IRC and helps ensure the availability of sufficient buffer against possible exogenous system-wide shocks. Under the Positive Neutral CCyB approach, authorities aim for a positive CCyB when risks are judged to be neither subdued nor elevated. For more information, see the Bank for International Settlements' "Newsletter on positive cycle-neutral countercyclical capital buffer rates" dated 5 October 2022 (https://www.bis.org/publ/bcbs_nl30.htm).

[61] These include measures of bank, corporate, and household leverage; debt servicing capacity; profitability, asset quality, and funding conditions within the banking sector; and macroeconomic imbalances.

[62] Under the new CCyB framework effective from 1 April 2024, the IRC will be the higher of two constituent components: a Composite CCyB Guide based on the credit-to-GDP gap and the property price-to-rent gap, and a Positive Neutral CCyB that sets a floor for the IRC.

Table 5.F
Information related to the Hong Kong jurisdictional countercyclical capital buffer

	18-Oct-24	Q2-2026	Q3-2026
Announced CCyB	0.5%		
Date effective	18-Oct-24		
Initial Reference Calculator	1.00%	1.00%	1.00%
Basel Common Reference Guide	0.00%	0.00%	0.00%
Property Buffer Guide	0.00%	0.00%	0.00%
Composite CCyB Guide	0.00%	0.00%	0.00%
Positive Neutral CCyB	1.00%	1.00%	1.00%
Primary gap indicators			
Credit/GDP gap	–35.2%	–38.4%	–36.6%
Property price/rent gap	–25.6%	–21.2%	–19.4%

Notes:

1. The values of all CCyB guides and their respective input variables are based on public data available prior to the corresponding review/announcement date, and may not be the most recently available as of each quarter end (refer to SPM CA-B-1 for explanations of the variables).
2. Following the revised CCyB framework as effective from 1 April 2024, the 2.5% cap is applied on the Composite CCyB Guide instead of the Basel Common Reference Guide and Property Buffer Guide (refer to SPM CA-B-1 for details of the formula and explanation).

Source: HKMA.

Key performance indicators of the banking sector are provided in Table 5.G.

Table 5.G
Key Performance Indicators of the Banking Sector[1] (%)

	Jun 2025	Mar 2026	Jun 2026
Interest rates			
1-month HIBOR fixing[2] (quarterly average)	1.88	2.47	2.59
3-month HIBOR fixing (quarterly average)	2.54	2.65	2.74
BLR[3] and 1-month HIBOR fixing spread (quarterly average)	3.37	2.53	2.41
BLR and 3-month HIBOR fixing spread (quarterly average)	2.71	2.35	2.26
Composite interest rate[4]	1.26	1.25	1.37
		All AIs	
Balance sheet developments[5]			
Total deposits	+4.0	+1.0	+3.9
Hong Kong dollar	+1.8	+1.9	+3.4
Foreign currency	+5.9	+0.3	+4.3
Total loans	+1.9	+3.0	+3.3
Domestic lending[6]	+1.6	+3.0	+3.0
Loans for use outside Hong Kong[7]	+2.6	+3.1	+4.4
Negotiable instruments			
Negotiable certificates of deposit (NCDs) issued	+5.2	+3.9	+11.5
Negotiable debt instruments held (excluding NCDs)	+8.3	+4.8	+5.8
Asset quality			
As a percentage of total loans[8]			
Pass loans	95.87	95.93	96.11
Special mention loans	2.16	2.20	2.07
Classified loans[9] (gross)	1.97	1.87	1.82
Classified loans (net)[10]	1.22	1.19	1.12
Overdue > 3 months and rescheduled loans	1.58	1.46	1.47
Classified loan ratio (gross) of Mainland related lending[11]	2.16	1.79	1.81
Liquidity ratios (consolidated)			
Liquidity Coverage Ratio — applicable to category 1 institutions (quarterly average)	172.8	160.2	150.5
Liquidity Maintenance Ratio — applicable to category 2 institutions (quarterly average)	66.3	66.6	67.0
Net Stable Funding Ratio — applicable to category 1 institutions	143.9	140.9	137.9
Core Funding Ratio — applicable to category 2A institutions	189.4	182.2	184.6
		Retail banks	
Profitability			
Loan impairment charges as a percentage of average total assets (year-to-date annualised)	0.18	0.09	0.14
Net interest margin (year-to-date annualised)	1.47	1.53	1.53
Cost-to-income ratio (year-to-date)	36.7	33.4	34.6
		Surveyed institutions	
Asset quality			
Delinquency ratio of residential mortgage loans	0.13	0.13	0.11
Credit card lending			
Delinquency ratio	0.40	0.39	0.36
Charge-off ratio — quarterly annualised	2.57	2.25	2.45
— year-to-date annualised	2.48	2.25	2.34
		All locally incorporated AIs	
Capital adequacy (consolidated)			
Common Equity Tier 1 capital ratio	19.9	20.3	19.6
Tier 1 capital ratio	22.3	22.8	22.1
Total capital ratio	24.4	24.9	24.2
Leverage ratio	7.9	7.9	7.5

Notes:

1. Figures are related to Hong Kong offices only except where otherwise stated.
2. The Hong Kong Interbank Offered Rates are released by the Hong Kong Association of Banks.
3. With reference to the rate quoted by The Hongkong and Shanghai Banking Corporation Limited.
4. The composite interest rate is a weighted average interest rate of all Hong Kong dollar interest-rate-sensitive liabilities, which include deposits from customers, amounts due to banks, negotiable certificates of deposit and other debt instruments, and all other liabilities that do not involve any formal payment of interest but the values of which are sensitive to interest rate movements (such as Hong Kong dollar non-interest bearing demand deposits) on the books of banks. Further details can be found on the HKMA website.
5. Quarterly change.
6. Loans for use in Hong Kong plus trade finance.
7. Including "others" (i.e. unallocated).
8. Figures are related to all AIs' Hong Kong offices, as well as locally incorporated AI's branches and major subsidiaries outside Hong Kong.
9. Classified loans are those loans graded as "substandard", "doubtful", or "loss".
10. Net of specific provisions/individual impairment allowances.
11. Figures are related to all AIs' Hong Kong offices, as well as locally incorporated AI's Mainland branches and subsidiaries.

Box 4
The implications of digitalisation adoption for Hong Kong non-financial corporates: An assessment based on textual analysis

Introduction[63]

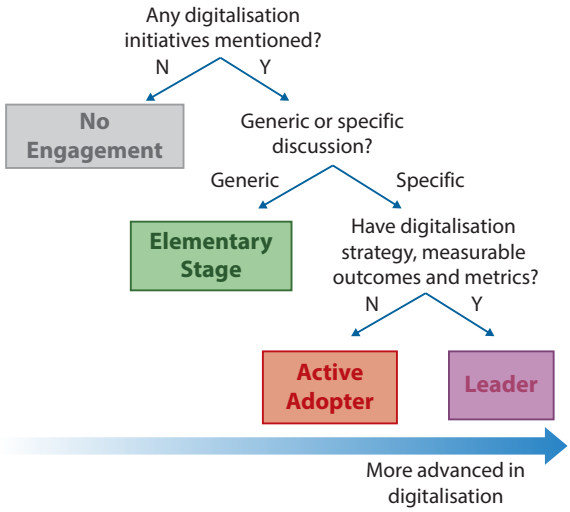
The rapid development of digital technology, particularly generative A.I. (GenA.I.), has prompted corporates worldwide to increasingly adopt the latest technologies to achieve efficiency gains and generate new value creation opportunities. While it may be too early to assess the full impact of firms' adoption of these cutting-edge technologies, digitalisation more broadly has been a long-term trend. Consequently, valuable lessons can be drawn from how digitalisation efforts in recent years have impacted corporates.

Against this backdrop, this box conducts a textual analysis to examine the extent of digitalisation adoption by non-financial corporates in Hong Kong in recent years and its implications for corporate performance and employment.[64]

Data sample and methodology

Since conventional financial data does not capture a firm's level of digitalisation adoption, this study leverages a GenA.I. tool to conduct textual analysis of annual reports and assess such adoption. The sample consists of 734 Hong Kong–listed corporates that are headquartered and operating in Hong Kong.[65] Based on the discussions regarding digitalisation initiatives in the annual reports of these corporates, we classify firms into four categories reflecting their level of engagement in digitalisation adoption, namely "*Leader*", "*Active Adopter*", "*Elementary Stage*", and "*No Engagement*". Specifically, the classification framework, as illustrated in Chart B4.1, considers whether firms have mentioned specific digitalisation projects or use cases, whether they have clear digitalisation strategies, and whether they report measurable outcomes of their digitalisation efforts.

Chart B4.1
Digitalisation adoption classification framework



The textual analysis employs a three-step process to classify firms into the above categories.

1) **Keyword extraction:** A keyword-based computer programming approach extracts relevant sections from each annual report that mention digitalisation initiatives.

2) **GenA.I. classification:** A GenA.I. model analyses the extracted sections and classifies each firm's level of digitalisation adoption for each fiscal year using a structured prompt.

[63] For details, please refer to Kong et al. (2025). "The implications of digitalisation adoption for Hong Kong non-financial corporates — An assessment based on textual analysis". *HKMA Research Memorandum*, 14/2025.

[64] It should be noted that this study discusses digitalisation more broadly, with the discussion not only confined to A.I. Thus, caution is warranted when interpreting the findings.

[65] The sample firms have annual reports available for all fiscal years from 2017 to 2024.

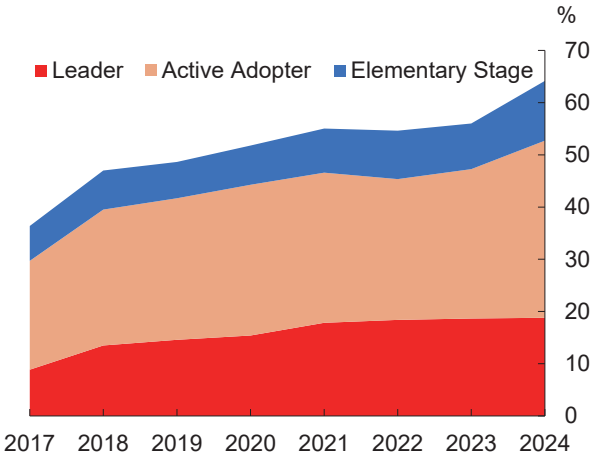
3) **Stability overlay:** To prevent spurious regression due to a temporary reporting lapse, when a firm's classification drops by one or more categories, we apply an overlay mechanism where we retain a firm's previous year's classification for the year of the classification drop. This assumes that a firm with established digital capabilities is unlikely to lose them in the short term, even if relevant initiatives are not repeatedly highlighted in every annual report.

Empirical analysis

Extent of digitalisation adoption

The textual analysis reveals that nearly two-thirds (64%) of the sample firms are currently engaged in digitalisation, up from around 49% in 2019. Over half (53%) are in more advanced stages (classified as *Leaders or Active Adopters*, and collectively classified as "more advanced firms"), up from 42% in 2019 (Chart B4.2).

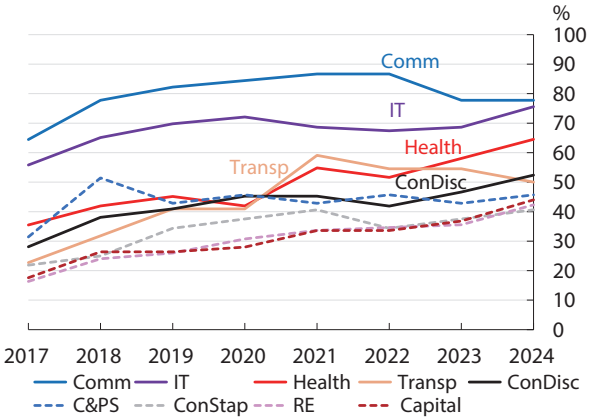
Chart B4.2
Share of firms adopting digitalisation



Sources: Firms' annual reports and HKMA staff calculation.

By sector, the communication services and information technology sectors are the most advanced, with over three-quarters of firms classified as *Leaders or Active Adopters* (Chart B4.3). This likely reflects their technology-focused nature. Importantly, many of these firms are also providers of technologies that enable other sectors to adopt digitalisation, such as providing data centres and software solutions.

Chart B4.3
Share of firms classified as *Leaders or Active Adopters*, by selected sector



Note: IT = information technology, Comm = communication services, ConDisc = consumer discretionary, Health = health care, Transp = transportation, Capital = capital goods, RE = real estate, C&PS = commercial and professional services, ConStap = consumer staples.

Sources: Firms' annual reports and HKMA staff calculation.

Following these, the health care, consumer discretionary, and transportation sectors are also more advanced than the rest of the economy. In particular, digitalisation adoption grew considerably since the COVID-19 pandemic for the health care and consumer discretionary sectors. This possibly reflects changes in consumer behaviour and new ways of delivering products and services, such as the growth of online shopping and video consultations, which also allow firms to use big data analytics for marketing and merchandising decisions.

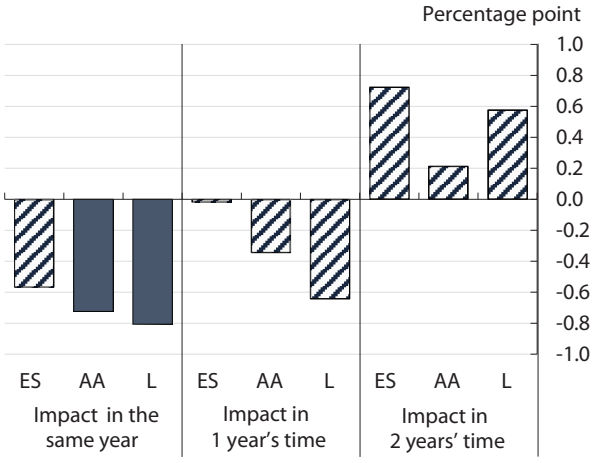
Meanwhile, a panel regression analysis shows that larger firms are more advanced in digitalisation adoption, likely because economies of scale enable them to afford the necessary investments and hiring.

Impact on corporate performance and employment

We estimate the impact of digitalisation adoption on three measures of corporate performance – return on assets (RoA), revenue growth, and price-to-book ratio (PB ratio) — using panel regression analysis.

The estimation results show that digitalisation adoption initially had a negative contemporaneous impact on RoA, with statistically significant reductions of 0.7–0.8 percentage points for *Active Adopters* and *Leaders* relative to *No Engagement* firms. This likely reflects the upfront costs of investment in intangible assets and increased hiring of relevant experts. The estimated impact turns positive after two years but is not statistically significant, suggesting that profitability benefits take time to materialise (Chart B4.4).

Chart B4.4
The estimated impact of digitalisation adoption on return on assets (%)

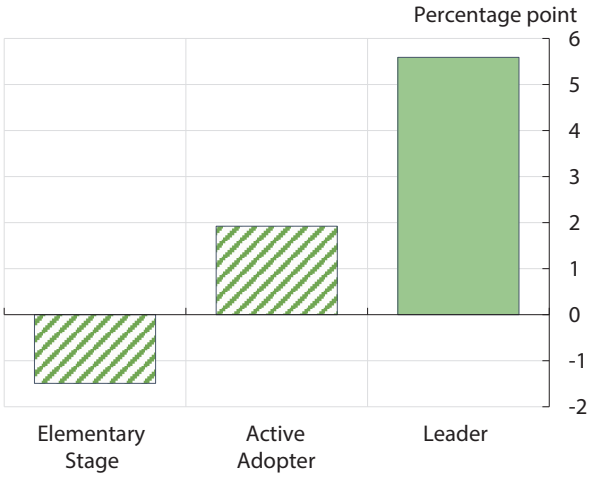


Notes:
1. Solid bars denote a statistically significant impact (at the 1%, 5%, or 10% level), relative to *No Engagement* firms.
2. ES = Elementary Stage, AA = Active Adopter, L = Leader.

Source: HKMA staff estimates.

Although digitalisation adoption did not appear to enhance profitability in the near term, we find that *Leaders* in digitalisation enjoyed higher revenue growth (by nearly six percentage points) when they embarked on digitalisation (Chart B4.5). Meanwhile, *Leaders* also enjoyed an uplift in their PB ratios of 0.3 units in the same period (Chart B4.6). This suggests that investors perceive better prospects for these firms, including higher profitability and a more resilient and sustainable business model in the longer term.

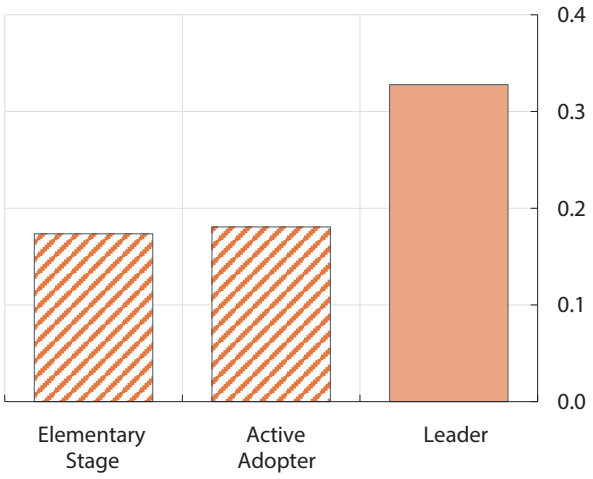
Chart B4.5
The estimated impact of digitalisation adoption on revenue growth, in the same year



Note: Solid bars denote a statistically significant impact (at the 1%, 5%, or 10% level), relative to *No Engagement* firms.

Source: HKMA staff estimates.

Chart B4.6
The estimated impact of digitalisation adoption on price-to-book ratio, in the same year



Note: Solid bars denote a statistically significant impact (at the 1%, 5%, or 10% level), relative to *No Engagement* firms.
Source: HKMA staff estimates.

Finally, we also look at the impact of digitalisation adoption on corporate employment. The results suggest that digitalisation adoption did not have a notable adverse impact on overall employment growth in the short term. In fact, more advanced firms saw higher growth, or a smaller decline, in employment, relative to *No Engagement* firms. It is, however, worth noting that digitalisation may have a heterogeneous impact across occupations, which is not captured by the dataset used in this study.[66]

Conclusion and implications

This study finds that digitalisation adoption among Hong Kong corporates has grown meaningfully in recent years, with nearly two-thirds of sample firms now engaged in digitalisation and over half in more advanced stages. Larger firms tend to be more advanced, possibly benefiting from economies of scale. Although digitalisation adoption had a negative short-term impact on profitability, the most advanced firms enjoyed higher revenue growth and an uplift in market valuations.

These findings underscore the importance for Hong Kong corporates to engage deeply in digitalisation to remain competitive and resilient. In addition, as larger firms tend to be more advanced, smaller firms face a greater risk of losing competitiveness. Targeted support for smaller firms such as small and medium-sized enterprises (SMEs) to adopt and invest in digital solutions is therefore warranted. The HKMA and the banking sector have launched several rounds of measures,[67] including offering credit products and services (such as loans with flexible repayment) to support SMEs in business expansion and their digital and green transformation.

Overall, this study offers ins ightful lessons learnt for assessing the implications of the latest A.I. technologies, although the findings should be interpreted with caution since the impact of A.I. may be more profound than digitalisation in the past.

[66] Our dataset does not allow for a breakdown of firm-level full-time employees by skillset. A thorough analysis of the impact on employees with different skillsets is beyond the scope of this study.

[67] For details of the SME support measures introduced by the HKMA and the banking sector, please visit the HKMA's Supporting SMEs webpage (https://www.hkma.gov.hk/eng/key-functions/banking/banking-regulatory-and-supervisory-regime/supporting-smes/).

Glossary of terms

Aggregate Balance
The sum of balances in the clearing accounts and reserve accounts kept with the central bank. In Hong Kong, this refers to the sum of the balances in the clearing accounts kept with the HKMA. The Aggregate Balance is a part of the Monetary Base.

Authorized Institution (AI)
An institution authorized under the Banking Ordinance to carry on the business of taking deposits. Hong Kong maintains a Three-tier Banking System, which comprises licensed banks, restricted licence banks and deposit-taking companies.

Best Lending Rate
A benchmark interest rate that banks use to price loans. In Hong Kong, the Best Lending Rate is used as a base for quoting interest rates on mortgage loans.

Certificates of Indebtedness (CIs)
Certificates issued by the Financial Secretary under the Exchange Fund Ordinance, to be held by note-issuing banks as cover for the banknotes they issue.

Composite Consumer Price Index
The main consumer price index (CPI) for Hong Kong. The Census and Statistics Department compiles three separate CPI series relating to households in different expenditure ranges. The CPI(A) relates to about 50% of households in the relatively low expenditure range; the CPI(B) relates to the next 30% of households in the medium expenditure range; and the CPI(C) relates to the next 10% of households in the relatively high expenditure range. The Composite CPI is compiled based on the aggregate expenditure pattern of all of the above households taken together.

Composite Interest Rate
The composite interest rate is a weighted average interest rate of all Hong Kong dollar interest-rate-sensitive liabilities, which include deposits from customers, amounts due to banks, negotiable certificates of deposit and other debt instruments, and all other liabilities that do not involve any formal payment of interest but the values of which are sensitive to interest rate movements (such as Hong Kong dollar non-interest bearing demand deposits) on the books of banks. Data from retail banks, which account for the majority of the Hong Kong dollar deposits in the banking sector, are used in the calculation. It should be noted that the composite interest rate represents only average interest expenses. There are various other costs involved in the making of a loan, such as operating costs (e.g. staff and rental expenses), credit cost and hedging cost, which are not covered by the composite interest rate.

Convertibility Undertaking (CU)
An undertaking by a central bank or Currency Board to convert domestic currency into foreign currency and vice versa at a fixed exchange rate. In Hong Kong, the HKMA operates Convertibility Undertakings on both the strong side and the weak side of the Linked Rate of 7.80. Under the strong-side Convertibility

Undertaking, the HKMA undertakes to buy US dollars from licensed banks at 7.75. Under the weak-side Convertibility Undertaking, the HKMA undertakes to sell US dollars at 7.85. Within the Convertibility Zone between 7.75 and 7.85, the HKMA may choose to conduct market operations consistent with Currency Board principles with the aim of promoting the smooth functioning of the money and foreign exchange markets.

Convertibility Zone

The Hong Kong dollar-US dollar exchange rate band, defined by the levels of the strong- and weak-side Convertibility Undertakings, within which the HKMA may choose to conduct market operations consistent with Currency Board principles.

Exchange Fund Bills and Notes (EFBNs)

Debt instruments issued by the HKMA for the account of the Exchange Fund. These instruments are fully backed by the foreign reserves. The HKMA has undertaken that new Exchange Fund paper will only be issued when there is an inflow of funds, thus enabling the additional paper to be fully backed by the foreign reserves. Since 1 April 1999, interest payments on Exchange Fund paper have been allowed to expand the Monetary Base. Additional Exchange Fund paper is issued to absorb such interest payments. This is consistent with the Currency Board discipline since interest payments on Exchange Fund paper are backed by interest income on the US dollar assets backing the Monetary Base.

Monetary Base

A part of the monetary liabilities of a central bank. The Monetary Base is defined, at the minimum, as the sum of the currency in circulation (banknotes and coins) and the balance of the banking system held with the central bank (the reserve balance or the clearing balance). In Hong Kong, the Monetary Base comprises Certificates of Indebtedness (for backing the banknotes issued by the note-issuing banks), government-issued currency in circulation, the sum of the balances of the clearing accounts kept with the HKMA (the Aggregate Balance), and Exchange Fund Bills and Notes.

Money supply

The total stock of money available in the economy. Hong Kong has three measures of money supply: Money Supply definition 1 (M1) is defined as the sum of legal tender notes and coins held by the public plus customers' demand deposits placed with licensed banks. Money Supply definition 2 (M2) is defined as M1 plus customers' savings and time deposits with licensed banks plus negotiable certificates of deposit (NCDs) issued by licensed banks held outside the banking sector. Money Supply definition 3 (M3) is defined as M2 plus customers' deposits with restricted licence banks and deposit-taking companies plus NCDs issued by these institutions held outside the banking sector.

Nominal and Real Effective Exchange Rate (NEER and REER)

An indicator of the overall exchange rate value of the Hong Kong dollar against a basket of currencies of Hong Kong's principal trading partners. The nominal effective exchange rate (NEER) is a weighted average of the exchange rates between Hong Kong and its principal trading partners. The real effective exchange rate (REER) is obtained by adjusting the NEER for relative movements in the seasonally adjusted consumer price indices of those selected trading partners.

Abbreviations

1m moving average	One-month moving average
3m moving average	Three-month moving average
3m-on-3m	Three-month-on-three-month
3mma	Three-month moving average
AB	Aggregate Balance
ADP	Automated date processing
AEs	Advanced economies
A.I.	Artificial Intelligence
AIs	Authorized institutions
AMCM	Monetary Authority of Macao
APAC	Asia-Pacific
API	Application Programming Interface
ASEAN	Association of Southeast Asian Nations
AU	Australia
AUD	Australian dollar
AUM	Assets under Management
BAU	Business-as-usual
bn	Billion
BLRs	Best Lending Rates
BoJ	Bank of Japan
bps	basis points
CAPEX	Capital expenditure
CAR	Capital Adequacy Ratio
CCPI	Composite Consumer Price Index
CCDC	China Central Depository & Clearing Co., Ltd.
CCyB	Countercyclical capital buffer
CDs	Certificates of deposits
CET1	Common equity tier-one
CEWC	Central Economic Work Conference
CFETS	China Foreign Exchange Trade System
CFR	Core Funding Ratio

CIBM	China Interbank Bond Market
CIs	Certificates of Indebtedness
CL	Confidence Level
CLR	Classified Loan Ratio
CMBS	Commercial mortgage-backed securities
CMU	Central Moneymarkets Unit
CN	Chinese Mainland
CNH	Offshore renminbi in Hong Kong
CNY	Onshore renminbi
COVID	Coronavirus Disease
CPI	Consumer Price Index
CRE	Commercial real estate
C&SD	Census and Statistics Department
CU	Convertibility Undertaking
DaR	Debt-at-risk
DBGS	Digital Bond Grant Scheme
DI	Direct investment
DID	Difference-in-differences
DLT	distributed ledger technology
DSR	Debt-servicing ratio
EA	Euro area
EBIT	Earnings before interest and taxes
EBITDA	Earnings before interest, taxes, depreciation and amortization
ECB	European Central Bank
EFBNs	Exchange Fund Bills and Notes
EIC	Electronic integrated circuit
EM	Emerging-market
EMEs	Emerging Market Economies
EPS	Earnings per share
ETFs	Exchange traded funds

EU	European Union
EUR	Euro
FDI	Foreign direct investment
Fed	Federal Reserve
FIC	Fixed Income and Currency
FINI	Fast Interface for New Issuance
FIMA	Foreign and International Monetary Authorities
FOMC	Federal Open Market Committee
FPS	Faster Payment System
FSTB	the Financial Services and the Treasury Bureau
FX	Foreign exchange
FYP	Five-Year Plan
GBA	Guangdong-Hong Kong-Macao Greater Bay Area (GBA)
GBP	British Pound Sterling
GDP	Gross Domestic Product
GDR	Granular Data Reporting
GEM	Growth Enterprise Market
GenA.I.	Generative Artificial Intelligence
GFC	Global Financial Crisis
GHG	Greenhouse gases
GICS	Global Industry Classification Standard
GVCs	Global value chains
G-SIBs	Global Systematically Important Banks
HHI	Herfindahl-Hirschman Index
HIBOR	Hong Kong Interbank Offered Rate
HK	Hong Kong
HKD	Hong Kong dollar
HKEX	The Hong Kong Exchanges and Clearing Limited
HKFRS	Hong Kong Financial Reporting Standard
HKMA	Hong Kong Monetary Authority
HKMC	Hong Kong Mortgage Corporation Limited

HKPC	Hong Kong Productivity Council
HK$M3	Hong Kong dollar broad money supply
HKSAR	Hong Kong Special Administrative Region
HS	Harmonized System
HSCEI	Hang Seng China Enterprises Index
HSI	Hang Seng Index
HY	high-yield
IBPS	Internet Banking Payment System
IC	Integrated circuits
ICR	Interest Coverage Ratio
ICSD	International Central Securities Depository
ID	Indonesia
IDR	Indonesian Rupiahs
I/E	Import/Export
IEEPA	International Emergency Economic Powers Act
IFC	International Finance Corporation
IIF	Institute of International Finance
IMF	International Monetary Fund
IPO	Initial Public Offering
IRC	Initial Reference Calculator
IT	Information technology
JP	Japan
JPY	Japanese Yen
KR	South Korea
KRW	South Korean Won
LCR	Liquidity Coverage Ratio
LIBOR	London Interbank Offered Rate
LERS	Linked Exchange Rate System
LFPR	Labour Force Participation Rate
lhs	Left-hand side
LLM	Large language model

LMR	Liquidity Maintenance Ratio
LNG	Liquefied natural gas
LPR	Loan Prime Rate
LR	Leverage Ratio
LTD	Loan-to-deposit
LTV	Loan-to-value
LWB	Labour and Welfare Bureau
mn	Million
MDBs	Multilateral Development Banks
MMFs	Money market funds
MVP	Minimum viable product
MIP	Mortgage Insurance Programme
MRF	Mutual Recognition of Funds
MY	Malaysia
MYR	Malaysian ringgit
MSCI	Morgan Stanley Capital International
NASDAQ	National Association of Securities Dealers Automated Quotations
NATO	North Atlantic Treaty Organisation
NBS	National Bureau of Statistics of China
NCD	Negotiable certificate of deposit
NEER	Nominal effective exchange rate
NFCs	Non-financial corporates
NFRA	National Financial Regulatory Administration
NIM	Net interest margin
NLP	Natural language processing
NPL	Non-performing loan
NSFR	Net Stable Funding Ratio
NZ	New Zealand
NZD	New Zealand dollar
OECD	Organisation for Economic Corporation and Development

OIS	Overnight indexed swap
OTC	Over-the-counter
p.a.	Per annum
P2P	Peer-to-peer
PBoC	People's Bank of China
PC	Private credit
PD	Probability of default
PH	The Philippines
PHP	Philippine Pesos
PMI	Purchasing Managers' Index
POEs	Private-owned enterprises
PPI	Producer Price Index
QDII	Qualified Domestic Institution Investor
QFI	Qualified Foreign Investor
qoq	Quarter-on-quarter
qoqa	Quarter-on-quarter annualised
R&VD	Rating and Valuation Department
RBF	RMB Business Facility
REER	Real effective exchange rate
Repo	Repurchase operation
rhs	Right-hand side
RMB	Renminbi
RML	Residential mortgage loan
ROA	Return on assets
ROE	Return on equity
RRR	Required reserve ratio
RTGS	Real Time Gross Settlement
RWA	Risk-weighted assets
SAFE	State Administration of Foreign Exchange
SDR	Special Drawing Rights
SFC	The Securities and Futures Commission

SFGS	SME Financing Guarantee Scheme
SG	Singapore
SGD	Singapore dollar
SHIBOR	Shanghai Interbank Offered Rate
SMEs	Small and medium-sized enterprises
SOEs	State-owned enterprises
SOFR	Secured Overnight Financing Rate
SOH	Strait of Hormuz
SPM	Supervisory Policy Manual
STCs	Specialist Technology Companies
SUR	Seemingly Unrelated Regression
S&P 500	Standard & Poor's 500 Index
TFP	Total factor productivity
TH	Thailand
THB	Thai Baht
th	Thousands
tn	trillion
TNA	Total net assets
TWI	Trade Weighted Index
UK	United Kingdom
UNCITRAL	United Nations Commission on International Trade Law
UNeDocs	United Nations electronic Trade Documents
US	United States
USD	US dollar
VAR	Vector Autoregression
VaR	Value-at-risk
VHSI	HSI Volatility Index
VIX	Chicago Board Options Exchange Market Volatility Index
wk	Week
WMP	Wealth management product
WTO	World Trade Organization
yoy	Year-on-year

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