Greater China — Week in Review

10 February 2025

Tommy Xie Dongming
Head of Asia Macro Research
xied@ocbc.com

Keung Ching (Cindy)
Greater China Economist
cindyckeung@ocbc.com

Highlights: AI hype outweighs the tariff risk

Despite President Trump's additional 10% tariff on Chinese imports, China's market sentiment remained buoyant, as optimism surrounding DeepSeek overshadowed concerns over escalating trade tensions. The Hang Seng Tech Index surged more than 9% since markets reopened after the Chinese New Year holiday. Meanwhile, the RMB held firm, with daily fixing kept stable below 7.17, indicating that China's policymakers remain committed to currency stability despite external pressures.

DeepSeek may not be revolutionary, however it has introduced three notable changes to the AI industry, signaling a shift in competitive dynamics. First, DeepSeek's ultra-low cost has been widely covered by global media. Second, Deepseek worked around the Nvidia's high level CUDA platform by using Nvidia's PTX (Parallel Thread Execution) language directly, an intermediate representation. This indicates that it's possible to "get closer to the metal" on Nvidia hardware without going through the usual CUDA pathways. This alternative for developers may also dilute the ecosystem control by Nvidia. Third, DeepSeek is open-source, reinforcing the notion that large language models (LLMs) are becoming depreciating assets.

Overall, the AI narrative is shifting from a focus on infrastructure development to real-world AI applications. While China lags behind the U.S. in cutting-edge AI breakthroughs, its strength in application layers offers a compelling opportunity for AI-driven economic gains. This raises optimism that AI adoption could benefit China's broader economy, potentially supporting growth over the next two years as AI-driven productivity gains scale across industries.

China's retaliatory tariff will take effect on February 10, following the unsuccessful attempt to arrange a call between President Xi and President Trump over the weekend. ￼ China's response to the latest round of U.S. tariffs has been measured and strategic, with no official confirmation yet on the exact impact on U.S. exports to China. While estimates vary, the affected trade volume is likely between $13 billion and $20 billion, which is significantly lower than the $50 billion worth of U.S. goods targeted during Trade War 1.0 in April 2018.

There are two key reasons behind this calibrated approach. First, China is opting for a more diversified response, utilizing non-tariff countermeasures such as export controls, regulatory investigations, and scrutiny of specific U.S. firms instead of relying solely on tariffs. This approach allows China to apply pressure in a more targeted and less disruptive manner.

Second, China appears to be leaving room for further negotiations. By keeping its response proportionate, China signals that while it is willing to retaliate, it remains open to dialogue, maintaining leverage in ongoing trade discussions.

While the immediate risks from the tariff are evident, China may also find opportunities in the broader application of tariffs. Higher tariffs on other countries may force U.S. firms to seek alternative suppliers. Given China's entrenched role in global supply chains post-Trade War 1.0, it could indirectly benefit from increased demand for alternative sourcing. U.S. protectionism could also accelerate China's regional cooperation efforts, reinforcing initiatives such as BRICS and the Belt and Road Initiative (BRI). This could strengthen China's economic influence in emerging markets, positioning it as a counterweight to U.S. trade policies.

Considering both direct and indirect effects, we estimate that the latest tariff announcements may lower China's GDP growth by 0.2%–0.3% in 2025. The full impact of the tariffs—originally expected in 2026—will now likely be brought forward to 2025 due to earlier-than-expected implementation.

While China has announced the retaliation, the bigger priority in Trade War 2.0 is subsidizing domestic consumers rather than overseas markets. As such, fiscal policy will likely play a more crucial role in 2025, focusing on stimulating domestic demand to counteract the effects of weakening external trade.

On domestic data, China's Consumer Price Index (CPI) accelerated to 0.5% YoY in January 2025, up from 0.1% YoY in December 2024, driven by Chinese New Year effects, as both food and service prices increased ahead of the holiday season. Despite the temporary boost, the rebound in CPI is unlikely to be sustainable. CPI is expected to contract by more than 0.5% YoY in February, following seasonal price corrections after the Chinese New Year holiday. For Q1 2025, inflation is likely to remain largely flat, with CPI potentially reaccelerating to around 1% in Q2. However, the broader disinflationary trend remains a challenge, signaling the need for more monetary policy support to anchor inflation expectations and stimulate demand.

Hong Kong's real GDP growth accelerated to 2.4% in the final quarter of 2024, from an upwardly revised 1.9% in the third quarter, due to a smaller drag from private consumption. For 2024 as a whole, Hong Kong's economy expanded by 2.5% YoY (2023: 3.2% YoY), largely aligned with market consensus, and slightly above our in-house forecast at 2.4%.

During the fourth quarter of 2024, private consumption expenditure contracted by a slower pace of 0.2% YoY (3Q24: -1.3%), as result of positive wealth effect created from the sharp rally in local equity market in late-September and a series of rate cuts. Growth in goods exports slowed further to 1.2%, while service exports paced up to 5.6% YoY (3Q24: 4.0% and 2.9%). On the flip side, gross domestic fixed capital formation fell by 0.9% YoY (3Q24: 5.7%).

Headwinds from China's economic slowdown and the elevated interest rate environment are likely to moderate after China's stimulus package and the Fed's pivot, yet "Trump 2.0" could risk a worsening of US-China relations, and thereby dealing a blow to Hong Kong's economic recovery. Our full year GDP growth forecast for 2025 is pitched at 2.2%, accounting for waning support from a low base.

The US administration indicated the 10% additional levy on all Chinese imports, which took effect last week, would also apply to Hong Kong's exports. As a response, the Hong Kong government planned to file a complaint with WTO, for violation of WTO rules and failing to recognize Hong Kong's status as a separate customs territory.

Under the tariff measures, products manufactured in Hong Kong will be liable for the extra levy. Hence, Hong Kong's domestic exports to US will bear the brunt of incremental tariff. In 2024, Hong Kong's total domestic exports to US stood at HK$5,908 million, accounting for 10.2% total domestic exports and 0.1% of total exports. Based on a set of assumptions and rough calculation, the total value added affected is around HK$510 million, which translates to roughly 0.02% of GDP.

While re-exports (HK$4,485 billion in 2024) and offshore trade (HK$5,109 billion in 2021) (trading services provided by local firms for non-local parties under which traded goods will not enter Hong Kong) are not directly affected by the additional tariffs on Hong Kong's exports, they are not entirely immune to the challenging environment amid the heightened US-China trade tensions.

By far, the impacts of tariffs on Hong Kong are seen as manageable, but chances are that this ongoing trade negotiation may still take a turn for the worst and result in further hike in tariff rate or other retaliatory measures.

Key Development	
Facts	**OCBC Opinions**
▪ China's retaliatory tariff will take effect on February 10, following the unsuccessful attempt to arrange a call between President Xi and President Trump over the weekend.	▪ China has announced retaliatory tariffs on 80 U.S. products, imposing a 15% tariff on 8 products and a 10% tariff on 10 products. These affected goods fall under three key categories of the Harmonized System (HS): Chapter 27 (Mineral fuels), Chapter 84 (Machinery), and Chapter 87 (Vehicles and parts). ▪ China's response to the latest round of U.S. tariffs has been measured and strategic, with no official confirmation yet on the exact impact on U.S. exports to China. While estimates vary, the affected trade volume is likely between $13 billion and $20 billion, which is significantly lower than the $50 billion worth of U.S. goods targeted during Trade War 1.0 in April 2018. ▪ There are two key reasons behind this calibrated approach. First, China is opting for a more diversified response, utilizing non-tariff countermeasures such as export controls, regulatory investigations, and scrutiny of specific U.S. firms instead of relying solely on tariffs. This approach allows China to apply pressure in a more targeted and less disruptive manner. ▪ Second, China appears to be leaving room for further negotiations. By keeping its response proportionate, China signals that while it is willing to retaliate, it remains open to dialogue, maintaining leverage in ongoing trade discussions.
▪ The US postal service initially suspended acceptance of international packages from China and Hong Kong but reversed this decision a day later. The initial suspension followed President Trump's executive order eliminating the de minimis exemption, which previously allowed packages valued under $800 to enter the U.S. without duties or inspections.	▪ The USPS gave no specific reason for the reversal but stated it would collaborate with Customs and Border Protection to implement a collection process for the new tariffs to avoid delivery disruptions. Overall, changing the de minimis policy in the U.S. generally requires congressional action because the threshold is set by law. President Trump would likely to continue to test the boundaries of presidential power but the change may also be swift once he hits the wall.
▪ Hong Kong: The US administration indicated the 10% additional levy on all Chinese imports, which took effect last week, would also apply to Hong Kong's exports. As a response, the Hong Kong government planned to file a complaint with WTO, for violation of WTO rules and failing to recognize Hong Kong's status as a separate customs territory.	▪ Under the tariff measures, products manufactured in Hong Kong will be liable for the extra levy. Hence, Hong Kong's domestic exports to US will bear the brunt of incremental tariff. In 2024, Hong Kong's total domestic exports to US stood at HK$5,908 million, accounting for 10.2% total domestic exports and 0.1% of total exports. Based on a set of assumptions and rough calculation, the total value added affected is around HK$510 million, which translates to roughly 0.02% of GDP. ▪ While re-exports (HK$4,485 billion in 2024) and offshore trade (HK$5,109 billion in 2021) (trading services provided by local firms for non-local parties under which traded goods will not enter Hong Kong) are not directly affected by the additional tariffs on Hong Kong's exports, they are not entirely immune to the challenging environment amid the heightened US-China trade tensions. ▪ By far, the impacts of tariffs on Hong Kong are seen as manageable, but chances are that this ongoing trade negotiation may still take a turn for the worst and result in further hike in tariff rate or other retaliatory measures.

Key Economic News	
Facts	**OCBC Opinions**
▪ China's Consumer Price Index (CPI) accelerated to 0.5% YoY in January 2025, up from 0.1% YoY in December 2024.	▪ On a sequential basis, CPI rose by 0.7% MoM, driven by Chinese New Year effects, as both food and service prices increased ahead of the holiday season. Service prices surged 0.9% MoM, while food prices rose 1.3% MoM. However, the increase in food prices was still weaker than the five-year holiday season average of 2.62% MoM, suggesting muted underlying demand. ▪ Despite the temporary boost, the rebound in CPI is unlikely to be sustainable. CPI is expected to contract by more than 0.5% YoY in February, following seasonal price corrections after the Chinese New Year holiday. For Q1 2025, inflation is likely to remain largely flat, with CPI potentially reaccelerating to around 1% in Q2. However, the broader disinflationary trend remains a challenge, signaling the need for more monetary policy support to anchor inflation expectations and stimulate demand. ▪ Meanwhile, China's Producer Price Index (PPI) fell 0.2% MoM in January, with the pace of decline expanding by 0.1 percentage points from the previous month. On a YoY basis, PPI contracted 2.3%, marking 28 consecutive months in negative territory. Producer goods prices turned from flat in December to a 0.2% decline, while consumer goods prices stabilized after a 0.1% decline previously, mainly due to a rebound in durable consumer goods prices. ▪ The prolonged PPI deflation reflects uneven transmission from strong industrial output to corporate profitability, suggesting that underlying economic pressures persist despite signs of cyclical stabilization. The persistent weakness in factory-gate prices reinforces expectations that China's policymakers may need to further ease monetary conditions to support business margins and domestic demand recovery.
▪ Hong Kong: Real GDP growth accelerated to 2.4% in the final quarter of 2024, from an upwardly revised 1.9% in the third quarter, due to a smaller drag from private consumption. On a seasonally adjusted basis, the economy reverted to growth at 0.8% QoQ (3Q: -0.1% QoQ). For 2024 as a whole, Hong Kong's economy expanded by 2.5% YoY (2023: 3.2% YoY), largely aligned with market consensus, and slightly above our in-house forecast at 2.4%.	▪ During the fourth quarter of 2024, private consumption expenditure contracted by a slower pace of 0.2% YoY (3Q24: -1.3%), as result of positive wealth effect created from the sharp rally in local equity market in late-September and a series of rate cuts. Growth in goods exports slowed further to 1.2%, while service exports paced up to 5.6% YoY (3Q24: 4.0% and 2.9%). On the flip side, gross domestic fixed capital formation fell by 0.9% YoY (3Q24: 5.7%). ▪ Headwinds from China's economic slowdown and the elevated interest rate environment are likely to moderate after China's stimulus package and the Fed's pivot, yet "Trump 2.0" could risk a worsening of US-China relations, and thereby dealing a blow to Hong Kong's economic recovery. Our full year GDP growth forecast for 2025 is pitched at 2.2%, accounting for waning support from a low base.
▪ Hong Kong's retail sales fell by a 9.7% YoY in December, partly reflecting the increased outbound travels by local residents. For 2024 as a whole, total retail sales decreased by 7.3% in value and 9.0% in volume compared with 2023.	▪ The lagged recovery of inbound tourism sector, change in consumption patterns, decline in household net wealth, and strong HKD continued to weigh on retail sales activities. We expect retail sales to stay weak in the next couple of months. ▪ If the property and stock markets failed to recover meaningfully, retail sales are forecast to fall further by a low single digit in 2025. Yet, if positive wealth effects stemming from asset market rallies are sustained, retail sales are expected to see a mild expansion of

	around 2%.

Macro Research

Selena Ling
Head of Research & Strategy
lingssselena@ocbc.com

Tommy Xie Dongming
Head of Asia Macro Research
xied@ocbc.com

Keung Ching (Cindy)
Hong Kong & Macau Economist
cindyckeung@ocbc.com

Herbert Wong
Hong Kong & Taiwan Economist
herberthtwong@ocbc.com

Lavanya Venkateswaran
Senior ASEAN Economist
lavanyavenkateswaran@ocbc.com

Ahmad A Enver
ASEAN Economist
ahmad.enver@ocbc.com

Jonathan Ng
ASEAN Economist
jonathanng4@ocbc.com

Ong Shu Yi
ESG Analyst
shuyiong1@ocbc.com

FX/Rates Strategy

Frances Cheung, CFA
Head of FX & Rates Strategy
francescheung@ocbc.com

Christopher Wong
FX Strategist
christopherwong@ocbc.com

Credit Research

Andrew Wong
Head of Credit Research
wongvkam@ocbc.com

Ezien Hoo, CFA
Credit Research Analyst
ezienhoo@ocbc.com

Wong Hong Wei, CFA
Credit Research Analyst
wonghongwei@ocbc.com

Chin Meng Tee, CFA
Credit Research Analyst
mengteechin@ocbc.com

thereof, as implemented in any jurisdiction. No member of the OCBC Group shall be liable or responsible for the compliance by you or any Relevant Entity with any law, rule, regulation, guidance or similar (including, without limitation, MiFID II, as implemented in any jurisdiction).

The information provided herein may contain projections or other forward looking statements regarding future events or future performance of countries, assets, markets or companies. Actual events or results may differ materially. Past performance figures are not necessarily indicative of future or likely performance.

Privileged / confidential information may be contained in this report. If you are not the addressee indicated in the message enclosing the report (or responsible for delivery of the message to such person), you may not copy or deliver the message and/or report to anyone. Opinions, conclusions and other information in this document that do not relate to the official business of OCBC Bank, BOS, OIR, OSPL and their respective connected and associated corporations shall be understood as neither given nor endorsed.

Co.Reg.no.: 193200032W