

Press Release

(embargoed until 4:30 p.m. on 10 August 2012)

Economic Situation in the Second Quarter of 2012 and Latest GDP and Price Forecasts for 2012

The Government released today (Friday) the Half-yearly Economic Report 2012, together with the preliminary figures on Gross Domestic Product for the second quarter of 2012.

The Government Economist, Mrs Helen Chan, described the economic situation in the second quarter of 2012 and provided the latest GDP and price forecasts for the year.

MAIN POINTS

- * The Hong Kong economy experienced another quarter of tepid growth, with real GDP up by 1.1% in the second quarter of 2012 over a year earlier, after a mild 0.7% growth in the first quarter (revised up from the earlier estimate of 0.4%). Merchandise exports remained sluggish amid the severe external headwinds and continued to weigh on economic growth. On the other hand, the domestic sector was still relatively resilient, thereby providing a buffer to overall economic performance. On a seasonally adjusted quarter-to-quarter comparison, real GDP dipped marginally by 0.1% in the second quarter, following a 0.6% growth in the first quarter (also revised up from the earlier estimate of 0.4%).
- * External trade stayed weak in the second quarter. The renewed deterioration of the eurozone sovereign debt crisis since May further dampened global economic sentiments. Hong Kong's total exports of goods thus posted a slight year-on-year decline of 0.4% in real terms even against a relatively low base of comparison in the same period of 2011. The year-on-year dip in exports to the EU enlarged further, while exports to the Mainland, the US and other Asian markets saw some relative improvement. Thanks to sustained vibrancy in inbound tourism, overall exports of services expanded further, though also decelerating to only a modest year-on-year increase of 2.1% in real terms.
- * The domestic sector held up relatively better and remained on the rise in the second quarter. Private consumption expenditure grew solidly by 3.7% in real terms over a year earlier, on the back of stable job conditions and improved incomes. Investment spending grew further by 5.7%, underpinned by a pick-up in private sector construction activity and hectic public sector infrastructure works, as well as continued growth in machinery and equipment acquisition.
- * The labour market remained in a state of full employment, with total employment reaching another record high. The seasonally adjusted unemployment rate came down to 3.2% in the second quarter. Thanks to a tight labour market and with the additional boost of statutory minimum wage

(SMW) implementation since May 2011, wages and earnings saw further notable growth. The median household income rose by 5.1% in the second quarter in nominal terms over a year earlier, or by 0.9% in real terms after discounting inflation. Over the same period, average employment earnings for the lowest decile of full-time employees rose even more, by 10.4% in nominal terms or 6.4% in real terms.

- * The local stock market plunged in May alongside overseas markets on growing concerns over a possible Greek exit from the eurozone and worsening debt situation in Spain, but recouped some lost ground in June upon the joint efforts by EU leaders to stabilise the crisis. The local property market likewise turned somewhat quieter, with more moderate price rises and thinner transaction volume towards the end of the second quarter.
- * Since the last review in May, the external environment turned abruptly for the worse. Downside risks in the global economy continued to loom large, amid the lingering concerns over an eventual Greek exit from the eurozone, the setback in the eurozone economy, and the fragile fiscal positions of many of its member states. The US economic recovery has lost some momentum in recent months, clouded further by the uncertainties in the election year and its “fiscal cliff”. The negative spillovers from the sluggishness of the advanced economies to Asia have also turned increasingly visible. Amid mounting headwinds to the global economy, the external environment would thus remain difficult and continue to overshadow Hong Kong’s export outlook in the near term. Yet with the Asian economies generally having sounder fundamentals and larger room for policy maneuvering, many of them including the Mainland have gradually eased their policy to support growth in recent months. This should hopefully render some support to the region’s demand.
- * With the overhang of the euro debt crisis, the latest Quarterly Business Tendency Survey indicated that large enterprises have taken a slightly more cautious attitude towards the near-term business outlook. Nonetheless, the domestic sector is expected to hold up better. The prevailing favourable job and income conditions should continue to bode well for local consumption demand in the near term. The sustained high level of infrastructure works, thriving inbound tourism, and the boost from the package of measures announced in the Budget should also continue to provide a firm buffer to the local economy.
- * Given the meagre outturn of a 0.9% year-on-year real economic growth in the first half of 2012, and that downside risks on the external front have risen when compared to the last review three months ago, the Hong Kong economy is poised to attain only a modest growth for 2012 as a whole. The forecast GDP growth for 2012 as a whole is thus revised from 1-3% in the May round to 1-2% in the current round.
- * Underlying consumer price inflation receded further in the second quarter to 5.1%, from 5.9% in the first quarter. Softer global food and commodity prices as well as receding Mainland inflation had led to a further deceleration of import

prices in recent months. Locally, the relative stabilisation of fresh-letting residential rentals in the latter part of 2011 had also resulted in a visible moderation in the rise in the private housing rental component of the Consumer Price Index. As aggregate demand weakens and imported inflation is also easing, Hong Kong's inflation looks set to taper further in the coming months. However, in cognisance of a somewhat slower-than-expected pace of easing in inflation so far this year, the forecast rates of headline and underlying consumer price inflation for 2012 as a whole are slightly revised upwards to 3.7% and 4.3% respectively, from 3.5% and 4% in the previous round.

DETAILS

GDP

According to preliminary data on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, real GDP continued to expand slowly by 1.1% in real terms in the second quarter of 2012 over a year earlier, after a 0.7% growth in the first quarter (revised from the earlier estimate of 0.4%), dragged by the sustained weakness in external trade. On a seasonally adjusted quarter-to-quarter comparison, real GDP shrank marginally by 0.1% in the second quarter, after a 0.6% growth in the preceding quarter (also revised from the earlier estimate of 0.4%) (*Chart*).

2. The latest figures on GDP and its major expenditure components up to the second quarter of 2012 are presented in *Table 1*. Developments in different segments of the economy in the second quarter of 2012 are described below.

External trade

3. *Total exports of goods* shrank slightly by 0.4% in real terms in the second quarter over a year earlier, narrowing from the 5.7% decline in the first quarter. The EU market remained the weakest spot, falling further at a double-digit year-on-year rate in the second quarter, while exports to the Mainland, US and other Asian markets saw some relative improvement on a year-on-year basis, though largely helped by the lower base of comparison in the same period of 2011. The sluggish final demand in the advanced markets also manifested itself in reduced intake of raw materials by many Asian economies, thereby restraining Hong Kong's exports to these regional markets. On a seasonally adjusted basis, total exports of goods fell by 3.7% in real terms in the second quarter over the preceding quarter.

4. *Exports of services* fared somewhat better, though also decelerating further to a modest year-on-year growth of 2.1% in real terms in the second quarter, from 2.9% in the first quarter. Exports of travel services continued to provide the key impetus, with visitor arrivals sustaining a double-digit year-on-year growth in the quarter. On the other hand, exports of trade-related services and transportation services saw only mild increases amid the still sluggish trade flows, while exports of financial and business services contracted modestly owing to subdued fund-raising

and cross-border financing activities. On a seasonally adjusted quarter-to-quarter comparison, exports of services dipped slightly by 0.3% in the second quarter.

Domestic sector

5. The domestic sector stayed rather resilient in the second quarter. On the back of the sustained buoyancy in employment and income conditions, *private consumption expenditure* (PCE) grew further by 3.7% in real terms over a year earlier. The growth deceleration from the 6.5% growth in the first quarter was mainly on account of a distinctly high base of comparison a year earlier. On a seasonally adjusted quarter-to-quarter comparison, private consumption expenditure grew by 0.6% in real terms in the second quarter, broadly similar to the growth pace in the first quarter. *Government consumption expenditure* grew solidly further by 3.5% in real terms in the second quarter over a year earlier.

6. *Overall investment spending* grew by 5.7% year-on-year in real terms in the second quarter, following the strong growth of 12.9% in the first quarter. The moderation was mainly affected by the slower year-on-year growth in machinery and equipment acquisition, at 5.7%, the latter partly reflecting the more cautious business sentiments amid the escalating euro debt crisis, but the difference in the base effects in the first and second quarters of 2011 was also a relevant factor. Nevertheless, private sector construction activity picked up during the quarter, while public sector infrastructure works grew further. As a result, overall building and construction expenditure expanded notably further by 12.4% in real terms in the second quarter.

The labour sector

7. The labour market remained in a state of full employment in the second quarter. With job creation continuing apace, total employment rose to another record high, thereby pushing the *seasonally adjusted unemployment rate* down to a low of 3.2% in the second quarter, from 3.4% in the first quarter. The *underemployment rate* likewise fell slightly further to 1.4%. Against the tight labour market conditions, labour wages and earnings saw further appreciable growth. In particular, the median household income rose by 5.1% in the second quarter in nominal terms over a year earlier, or by 0.9% in real terms after discounting inflation. Over the same period, average employment earnings for the lowest decile of full-time employees rose even more, by 10.4% in nominal terms or 6.4% in real terms.

The asset markets

8. The *local stock market* exhibited sharp fluctuations along with other major overseas markets during the second quarter. With the renewed deterioration of the eurozone sovereign debt crisis on entering May, the Hang Seng Index plunged in May and early June, only to rebound subsequently on joint efforts by EU leaders to stem the crisis, closing the quarter at 19 441, down 5% from end-March 2012 but

still 5% higher than the level at end-2011.

9. The *residential property market* saw thinner trading during the second quarter on more cautious market sentiment amid the worsening euro debt crisis and subsequent global stock market gyrations. Residential property prices also turned more steady towards the end of the quarter, though still up by a cumulative 4% between March and June 2012. Overall flat prices in June surpassed the 1997 peak by around 16%. Meanwhile, flat rentals rebounded by 5% during the second quarter, and office and shop rentals also went up further by 2% and 6% respectively.

Prices

10. Consumer price inflation continued to taper in the second quarter along with receding price pressures from both the domestic and external sources. Locally, the relative stabilisation of fresh-letting residential rentals in the latter part of 2011 resulted in a moderated increase in the private housing rental component of the Consumer Price Index. Externally, the softening of global food and commodity prices and slower inflation in Hong Kong's major trading partners together helped alleviate imported inflation. Thus, with the peaking out of food prices and private housing rentals (which account for over half of the household consumption basket), *headline consumer price inflation* went down to 4.2% in the second quarter, from 5.2% in the first quarter. Netting the effects of the Government's relief measures, *underlying consumer price inflation* also receded to 5.1% in the second quarter, from 5.9% in the previous quarter.

Latest GDP and price forecasts for 2012

11. Since the last review in May, the external environment turned abruptly for the worse. Downside risks in the global economy continued to loom large, amid the lingering concerns over an eventual Greek exit from the eurozone, the setback in the eurozone economy, and the fragile fiscal positions of many of its member states. The US economic recovery has lost some momentum in recent months, clouded further by the uncertainties in the election year and its "fiscal cliff". The negative spillovers from the sluggishness of the advanced economies to Asia have also turned increasingly visible. Amid mounting headwinds to the global economy, the external environment would thus remain difficult and continue to overshadow Hong Kong's export outlook in the near term. Yet with the Asian economies generally having sounder fundamentals and larger room for policy maneuvering, many of them including the Mainland have gradually eased their policy to support growth in recent months. This should hopefully render some support to the region's demand.

12. With the overhang of the euro debt crisis, the latest Quarterly Business Tendency Survey indicated that large enterprises have taken a slightly more cautious attitude towards the near-term business outlook. Nonetheless, the domestic sector is expected to hold up better. The prevailing favourable job and income conditions should continue to bode well for local consumption demand in the near term. The

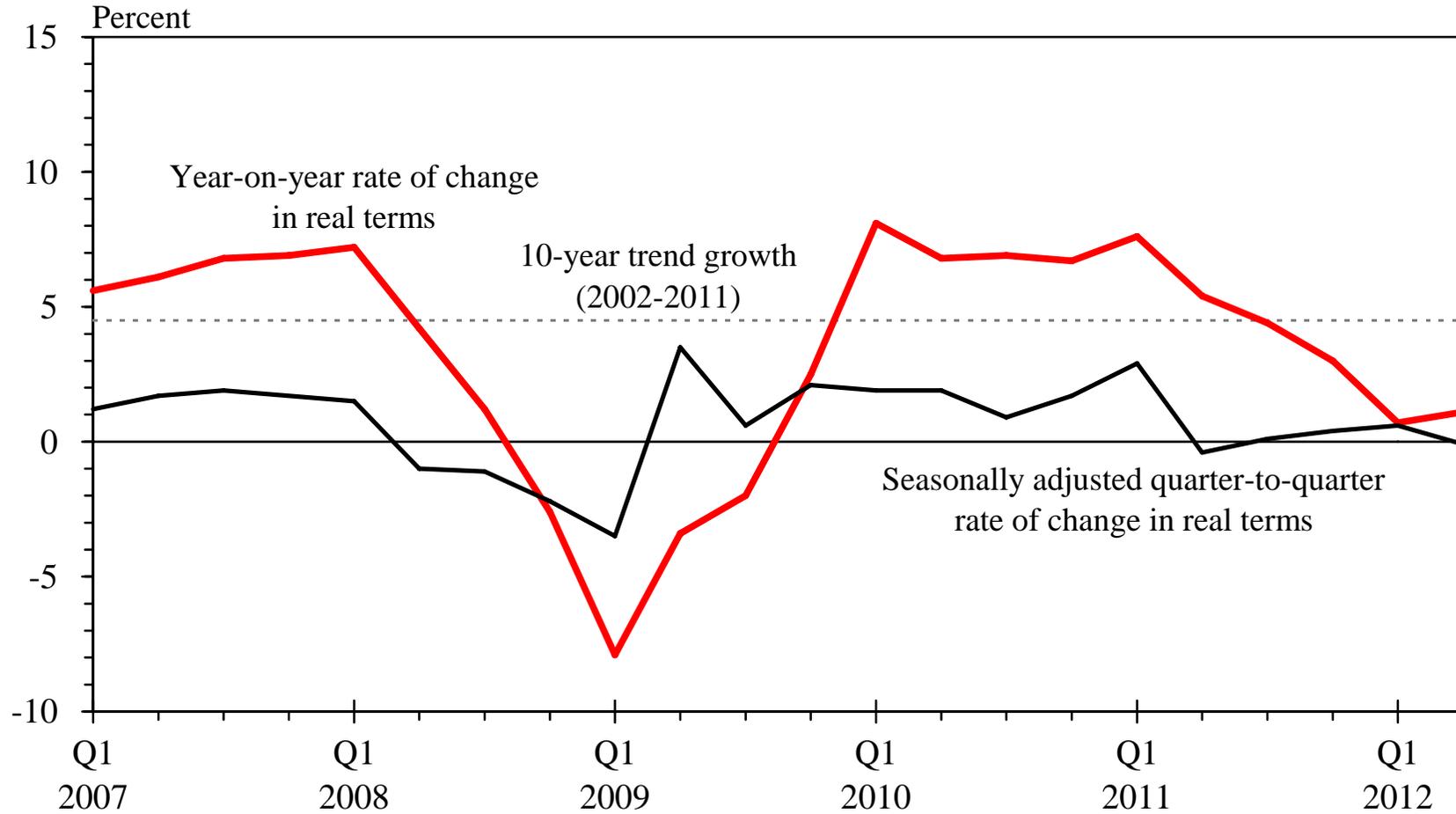
sustained high level of infrastructure works, thriving inbound tourism, and the boost from the package of measures announced in the Budget, should also continue to provide a firm buffer to the local economy.

13. Given the meagre outturn of a 0.9% year-on-year real economic growth in the first half of 2012, and that downside risks on the external front have risen when compared to the last review three months ago, the Hong Kong economy is poised to attain only a modest growth for 2012 as a whole. The forecast GDP growth for 2012 as a whole is thus revised from 1-3% in the May round to 1-2% in the current round (*Table 2*). For reference, the latest forecasts by private sector analysts mostly range from 1.5-2.5%, averaging at around 2.2%.

14. On inflation outlook, as aggregate demand weakens and imported inflation is also easing, Hong Kong's inflation looks set to taper further in the coming months. However, in cognizance of a somewhat slower-than-expected pace of easing in inflation so far this year, the forecast rates of headline and underlying consumer price inflation for 2012 as a whole are slightly revised upwards to 3.7% and 4.3% respectively, from 3.5% and 4% in the previous round (*Table 2*).

(The Half-yearly Economic Report 2012 is now available for online download, free of charge at <http://www.hkeconomy.gov.hk/en/reports/index.htm>. The print version is available for sale at \$110 per issue, plus postage charge. Users can purchase the print version online at the Government Bookstore at <http://www.bookstore.gov.hk>, or by calling the Publications Sales Unit of the Information Services Department at 2537 1910. The Report of the Gross Domestic Product, Second Quarter 2012, which contains the GDP figures up to the second quarter of 2012, is also available for online download, free of charge at the homepage of the Census and Statistics Department, <http://www.censtatd.gov.hk>.)

Hong Kong's Gross Domestic Product



Note : Figures for the second quarter of 2012 are preliminary estimates.

Table 1

**Gross Domestic Product and its main expenditure components
and the main price indicators
(year-on-year rate of change (%))**

	<u>2010[#]</u>	<u>2011[#]</u>	<u>2011</u>				<u>2012</u>	
			<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1[#]</u>	<u>Q2⁺</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>								
Private consumption expenditure	6.7	8.5	8.0 (0.7)	9.9 (3.3)	9.5 (1.6)	6.6 (0.8)	6.5 (0.7)	3.7 (0.6)
Government consumption expenditure	2.8	1.8	2.5 (1.7)	1.0 (-0.8)	1.3 (1.0)	2.2 (0.4)	2.3 (1.6)	3.5 (0.5)
Gross domestic fixed capital formation	7.7	7.6	0.7	7.7	11.7	9.8	12.9	5.7
<i>of which :</i>								
Building and construction	5.6	5.7	17.8	-4.2	3.0	7.6	12.6	12.4
Machinery, equipment and computer software	6.4	13.7	-11.2	17.8	26.7	20.5	23.3	5.7
Total exports of goods	17.3	3.6	16.8 (10.1)	0.3 (-9.5)	-2.2 (0.7)	2.0 (1.5)	-5.7 (1.8)	-0.4 (-3.7)
Imports of goods	18.1	4.8	12.6 (8.6)	2.6 (-5.1)	1.4 (-0.2)	3.9 (0.9)	-2.7 (1.7)	0.7 (-1.5)
Exports of services	14.6	6.7	9.0 (3.5)	7.4 (0.6)	5.3 (0.4)	5.3 (0.7)	2.9 (1.2)	2.1 (-0.3)
Imports of services	10.4	3.1	5.6 (-0.2)	2.9 (0.3)	1.4 (-0.5)	2.8 (3.2)	3.5 (0.4)	1.5 (-1.5)
Gross Domestic Product	7.1	5.0	7.6 (2.9)	5.4 (-0.4)	4.4 (0.1)	3.0 (0.4)	0.7 (0.6)	1.1 (-0.1)
<i>Change in the main price indicators (%)</i>								
GDP deflator	0.2	3.7	1.3 (1.3)	4.9 (1.4)	4.8 (2.0)	3.7 (-1.1)	3.5 (1.0)	2.5 (0.7)
Composite CPI								
Headline	2.4	5.3	3.8 (1.8)	5.2 (1.8)	6.4 (-0.9)	5.7 (3.0)	5.2 (1.3)	4.2 (0.9)
Underlying[^]	1.7	5.3	3.7 (1.8)	5.0 (1.7)	6.1 (1.5)	6.4 (1.2)	5.9 (1.3)	5.1 (1.0)
<i>Change in nominal GDP (%)</i>	7.3	8.9	9.0	10.6	9.4	6.8	4.2	3.6

Notes : Figures are subject to revision later on as more data become available. Seasonally adjusted quarter-to-quarter rate of change is not applicable to gross domestic fixed capital formation, as no clear seasonal pattern is found for the category due to the presence of considerable short term fluctuations.

(#) Revised figures.

(+) Preliminary figures.

() Seasonally adjusted quarter-to-quarter rate of change.

(^) After netting out the effects of Government's one-off relief measures.

Table 2**Economic forecasts for 2012
(rate of change (%))**

	Forecasts for 2012 as released <u>on 11.5.2012</u> (%)	Latest forecasts for 2012 <u>on 10.8.2012</u> (%)
Gross Domestic Product (GDP)		
<i>Real GDP</i>	1 to 3	<i>1 to 2</i>
<i>Nominal GDP</i>	2.5 to 4.5	<i>3 to 4</i>
Composite Consumer Price Index (CCPI)		
<i>Headline CCPI</i>	3.5	3.7
<i>Underlying CCPI</i>	4	4.3