

Outlook for the Hong Kong economy in 2015

2.19 Hong Kong's economic performance, as always, hinges on global economic and financial conditions. On the external front, the performance of Hong Kong's *exports of goods* has been mostly lacklustre amid the fragile global recovery in the aftermath of the Global Financial Crisis. In 2015, the export outlook remains rather bleak. The subdued growth in the eurozone and Japan will remain the major hindrance to global economic expansion, weighing on global trade flows. The weak demand conditions of some advanced economies will likely cast an adverse impact on production and trading activities in Asian economies, including the Mainland, with some possible spillovers to Hong Kong. Also, the strength of US dollar will not bode well for our overall export competitiveness, and in particular, the distinct weakness of the euro and yen will directly curtail our exports to Europe and Japan. Yet, better prospects for the US economy and the sounder economic fundamentals in Asia in general should hopefully provide some cushion against the headwinds in other parts of the global economy. There may also be some upside potential if the US economy were to pick up faster than expected, to the benefit of Asia's trade flows.

Diagram 2.5 : Hong Kong's exports of goods will continue to hinge on global economic conditions in 2015

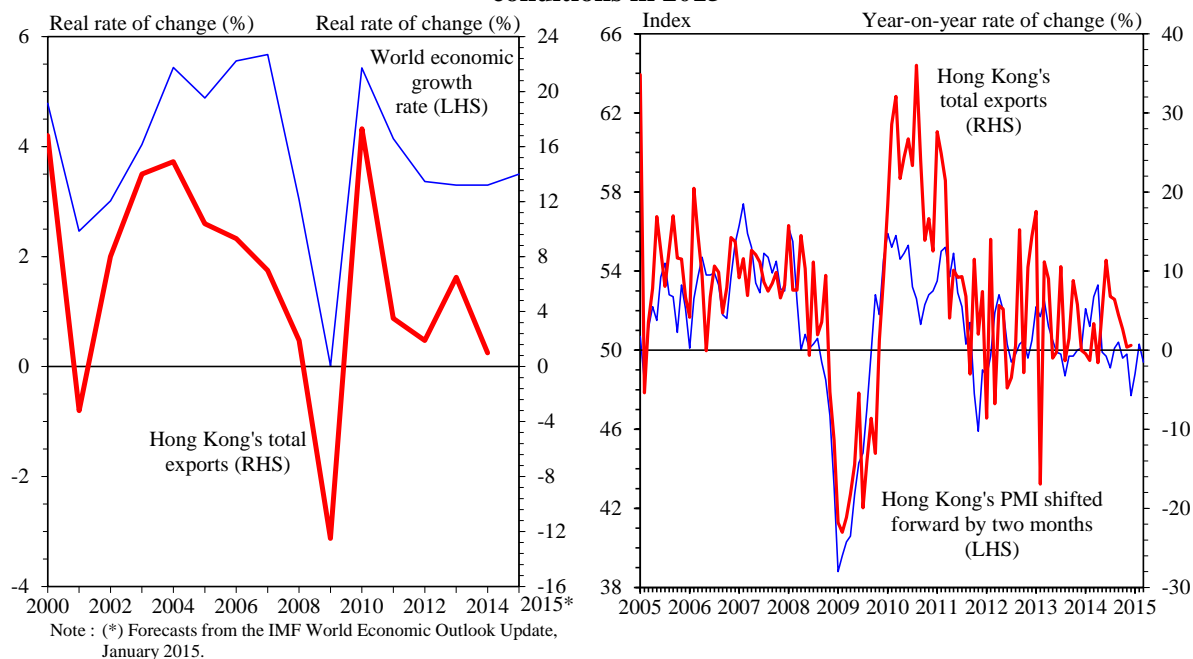
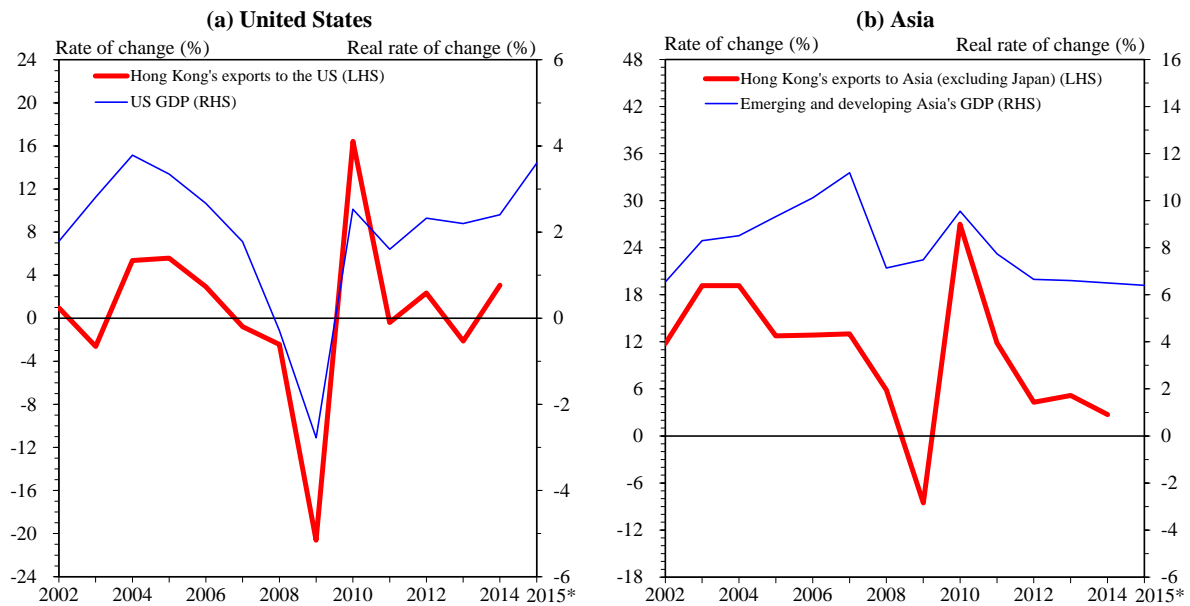


Diagram 2.6 : Regional trade is likely to be supported by the steady growth of the Mainland economy

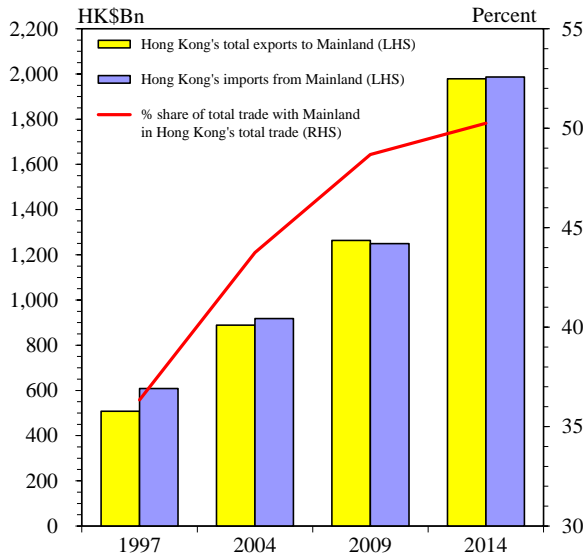


Note : (*) Forecasts from the IMF World Economic Outlook Update, January 2015.

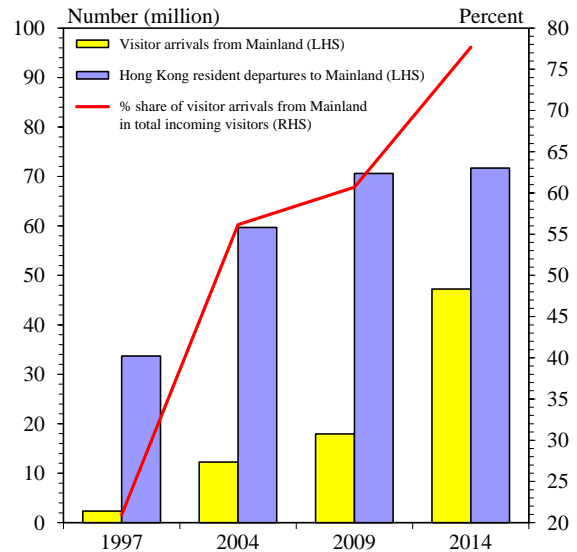
2.20 *Exports of services* look relatively more promising and should see better growth outlook in 2015 after a rather weak year in 2014. Exports of travel services are likely to show some improvement as the continued visible increase in visitors from the Mainland should provide solid support to inbound tourism. As to other services exports, exports of financial and business services will continue to benefit from the expansion of fund-raising and cross-border financial activities. On the other hand, in face of the choppy global trading environment, the outlook for exports of trade-related services and transportation services is not as promising, and growth will likely be modest at best. Yet, on balance, overall services exports should still stage a relative improvement this year.

Diagram 2.7 : Economic links with the Mainland are important for Hong Kong

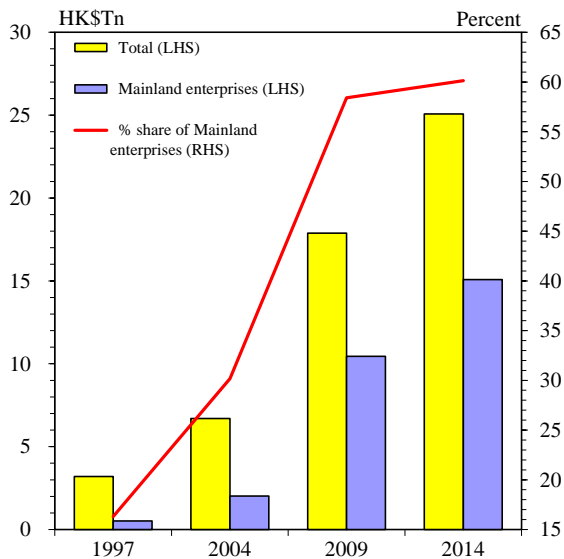
(a) Merchandise trade



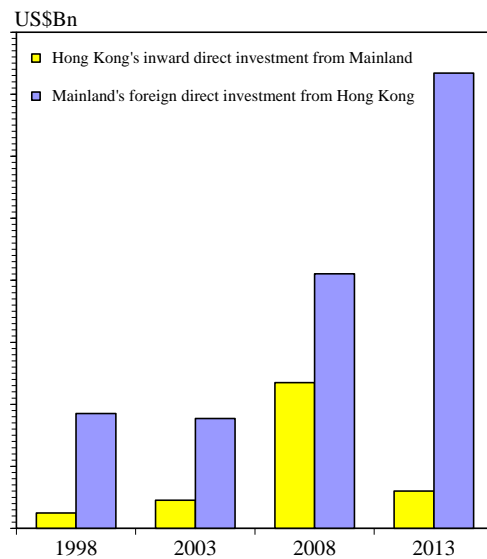
(b) Visitor arrivals from Mainland and Hong Kong resident departures to Mainland



(c) Market capitalisation of Mainland enterprises in the Hong Kong stock market (end-year figures)



(d) Mainland's foreign direct investment from Hong Kong and Hong Kong's inward direct investment from Mainland



2.21 Given the rather unpromising outlook for the external sector in 2015, this year's growth driver of our economy has to rely on the domestic sector, which has shown much resilience over the past years, helping to cushion the economy against the adverse external shocks. Although *domestic demand* slowed in 2014 following a prolonged period of below-trend GDP growth, private consumption expenditure should be able to hold up and see further growth in 2015, on the back of a resilient labour market and rising incomes, and more so, if asset market conditions were to remain supportive. The outlook for investment expenditure, on the other hand, is a bit more uncertain. In face of a still-highly unsteady global economic environment, investment could continue

to see volatility during the year, especially if interest rate outlook remained uncertain, and if local political disputes were to linger on. Indeed, the results of the latest Quarterly Business Tendency Survey on large enterprises and a consultation exercise on small and medium-sized enterprises (SMEs) both indicated that business sentiment about the near-term outlook remained rather cautious, though hiring sentiment stayed robust of late. Public construction works look set for further expansion, and hopefully would be able to provide a more stable growth source for overall investment in 2015.

Diagram 2.8 : Private consumption should see further growth as supported by steady employment conditions in the near term

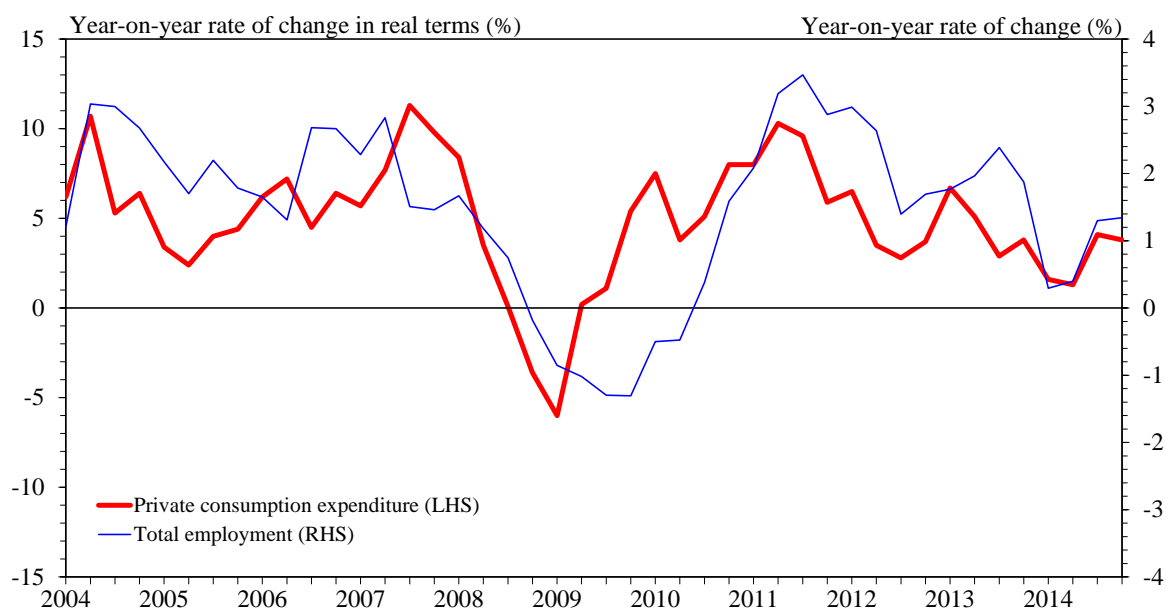


Diagram 2.9 : Consumer sentiment could hold up further if asset market conditions stayed supportive
 (a) Housing wealth (b) Equity wealth

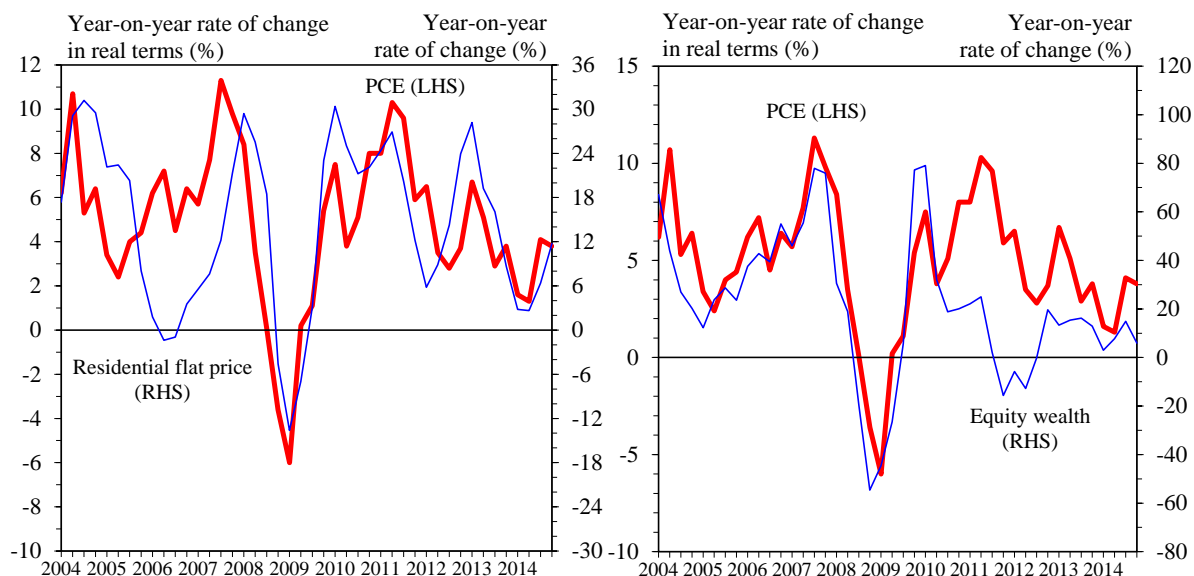
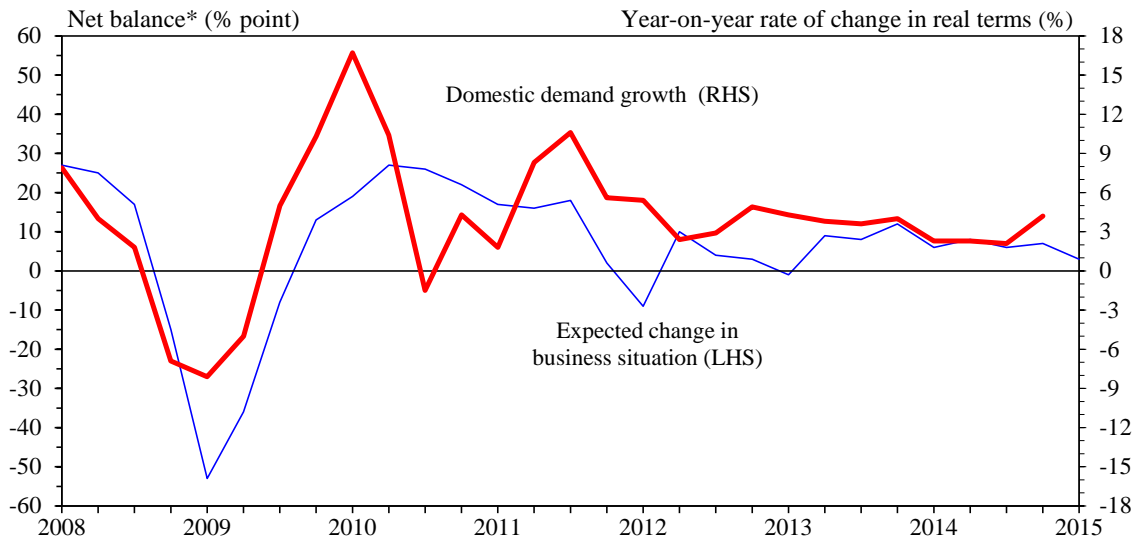
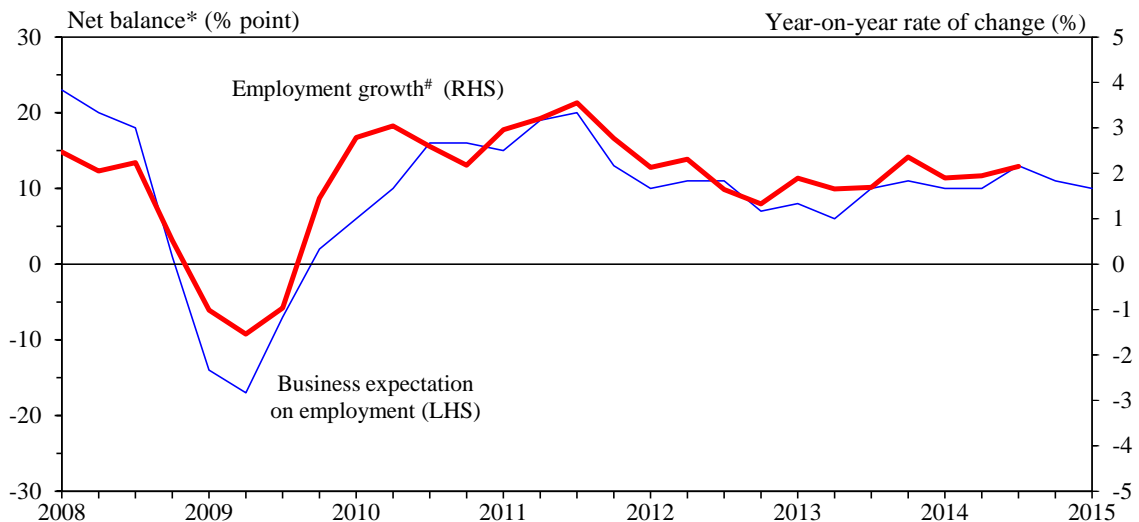


Diagram 2.10 : Business sentiment remained cautious about the near-term outlook



Note : (*) Net balance indicates the direction of expected change in business situation versus preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "better" over that choosing "worse". A positive sign indicates a likely upward trend while a negative sign, a likely downward trend.

Diagram 2.11 : Hiring sentiment stayed positive

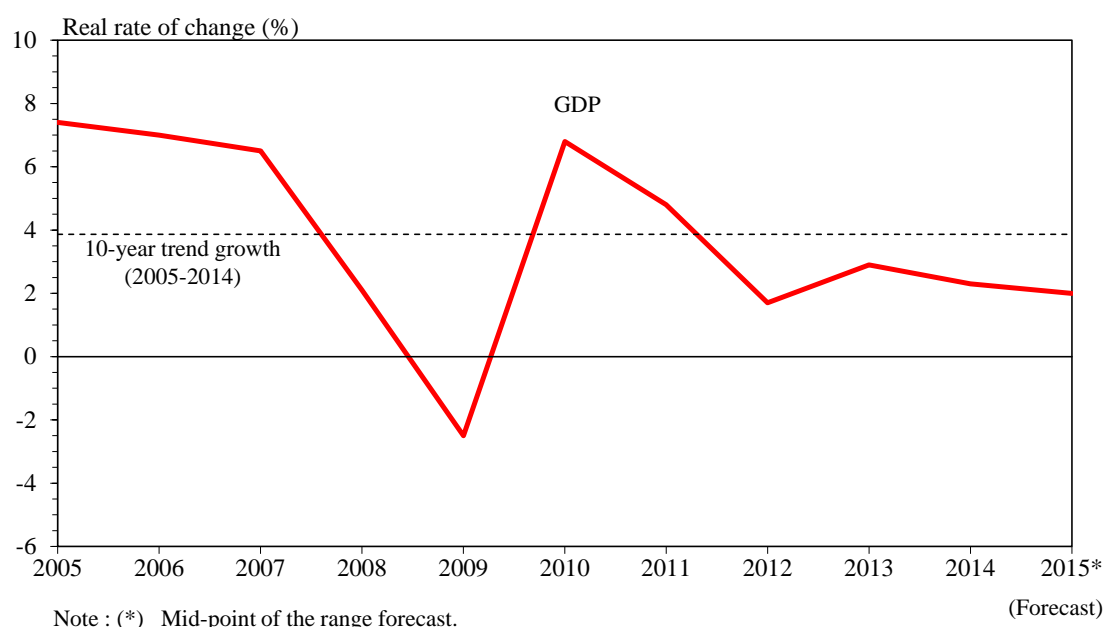


Notes : (*) Net balance indicates the direction of expected change in number of persons engaged versus preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "up" over that choosing "down". A positive sign indicates a likely upward trend while a negative sign, a likely downward trend.
 (#) Employment in private sector.

2.22 Taking into account the likely subdued performance of external demand and the relative resilient domestic demand, the Hong Kong economy is projected to expand by 1-3% in 2015, after the 2.3% growth in 2014 and compared to the average annual growth of 3.9% in the past ten years. The official forecast adopts a two-percentage-point range in view of the prevailing uncertainties surrounding the already-modest prospects for the global economy and the expected heightened volatility in global monetary conditions. Needless to say, downside risks still abound from the external front. Abrupt changes to

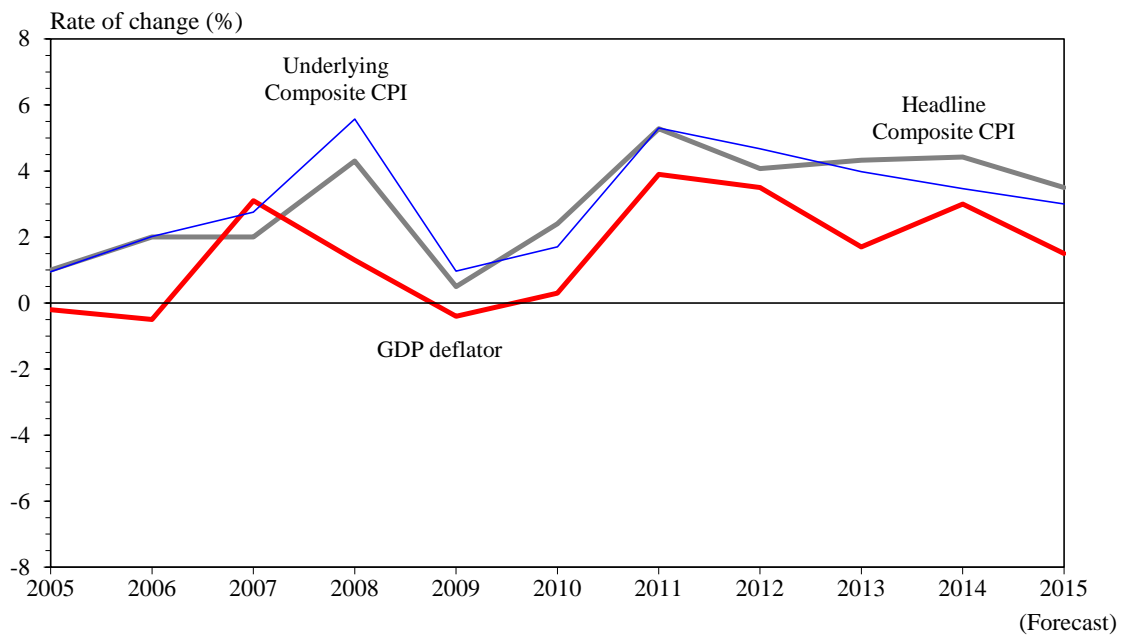
the global economic and financial conditions stemming from the different monetary policy stances of major central banks could trigger corrections in asset markets, in turn adversely denting consumption and investment sentiments. Moreover, the austere global economic environment could impact severely on some emerging market economies with weak fundamentals and thereby derail the global recovery. Nonetheless, there may be some upside potential to the forecast if global growth turns out to be stronger than expected, particularly if Asian economies are more resilient than envisaged despite the sluggishness in the advanced economies. For comparison, the prevailing forecasts by the private sector analysts for Hong Kong's economic growth in 2015 mostly fall within the range of 2.1-3.3%, averaging around 2.7%.

Diagram 2.12 : Economy expected to grow moderately further, but uncertainties still abound



2.23 Underlying inflation in Hong Kong fell further from 4.0% in 2013 to 3.5% in 2014. Price pressures will likely remain modest in 2015 amid the sub-par local economic growth and soft imported inflation. Externally, imported inflation looks set to remain tame, thanks to lower global inflation and soft international commodity prices. Locally, the moderate increases in commercial rentals during most of 2014, as well as the steady wage cost pressures, are both conducive to lower inflation pressures in 2015. Granting no unpleasant upside surprises in international commodity prices, *underlying Composite CPI* is forecast to increase by 3% for 2015 as a whole, down further from the 3.5% increase in 2014. Taking into account the effects of the Government's one-off measures, *headline Composite CPI* is forecast to increase by 3.5% in 2015, after 4.4% in 2014. The *GDP deflator* is forecast to rise by 1.5%, taking into account the expected slower increases in prices from both the local and external fronts.

Diagram 2.13 : Inflation is expected to ease further in 2015



Forecast rate of change in 2015 (%)

Gross Domestic Product (GDP)

<i>Real GDP</i>	1 to 3
<i>Nominal GDP</i>	2.5 to 4.5
<i>Per capita GDP in real terms</i>	0.2 to 2.1
<i>Per capita GDP at current market prices</i>	HK\$315,200-321,400 (US\$40,400-41,200)

Composite Consumer Price Index

<i>Headline</i>	3.5
<i>Underlying</i>	3

GDP Deflator	1.5
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**Forecast on Hong Kong's GDP growth in 2015
recently made by other selected parties**

The University of Hong Kong	(%) 2.3 to 3.3
Average forecast by private sector analysts [#]	2.7

Note : (#) Forecast GDP growth rates by private sector analysts mostly fall between 2.1% and 3.3%.

ECONOMIC PERFORMANCE IN 2014

1. Estimated rates of change in the Gross Domestic Product and its expenditure components and in the main price indicators in 2014:

	(%)
(a) Growth rates in real terms of:	
Private consumption expenditure	2.7
Government consumption expenditure	3.1
Gross domestic fixed capital formation	-0.3
<i>of which :</i>	
Building and construction	6.5
Machinery, equipment and intellectual property products	-5.2
Total exports of goods	1.0
Imports of goods	1.0
Exports of services	0.5
Imports of services	1.9
Gross Domestic Product (GDP)	2.3
<i>Per capita GDP in real terms</i>	1.6
<i>Per capita GDP at current market prices</i>	HK\$310,100 (US\$40,000)
(b) Rates of change in:	
Underlying Composite Consumer Price Index	3.5
GDP Deflator	3.0
Government Consumption Expenditure Deflator	4.6
(c) Growth rate of nominal GDP	5.3

2. Annual growth rates in real terms of re-exports and domestic exports based on external trade quantum index numbers:

	<i>Re-exports</i> (%)	<i>Domestic exports</i> (%)
2012	0	-13
2013	3	-9
2014	2	5
<i>Share in the value of total exports of goods in 2014</i>	98	2

3. Annual growth rates in real terms of retained imports by type:

<i>Retained imports</i>						
	<i>Total</i> (%)	<i>Consumer goods</i> (%)	<i>Foodstuffs</i> (%)	<i>Capital goods</i> (%)	<i>Raw materials and semi-manufactures</i> (%)	<i>Fuels</i> (%)
2012	4	6	2	22	-6	-7
2013	6	3	9	22	-3	0
2014	5	8	5	-7	13	-6

4. Annual growth rates in real terms of retained imports of capital goods by type:

<i>Retained imports of capital goods</i>					
	<i>Total</i> (%)	<i>Office equipment</i> (%)	<i>Industrial machinery</i> (%)	<i>Construction machinery</i> (%)	<i>Telecommunications equipment</i> (%)
2012	22	22	-26	-26	100
2013	22	9	-24	57	52
2014	-7	-69	28	-9	15

5. Annual growth rates in real terms of exports of services by type:

Exports of services

	<i>Total</i> (%)	<i>Trade-related services</i> (%)	<i>Transportation services</i> (%)	<i>Travel services</i> (%)	<i>Finance, insurance, business and other services</i> (%)
2012	2	1	-4	10	3
2013	5	1	-2	18	2
2014	0	1	2	-3	1

6. Hong Kong's visible and invisible trade balance in 2014 reckoned on GDP basis ^(Note 1):

	(HK\$ billion)
Total exports of goods	3,878.6
Imports of goods	4,471.8
<i>Visible trade balance</i>	-593.2
Exports of services	1,076.9
Imports of services	481.2
<i>Invisible trade balance</i>	595.7
<i>Combined visible and invisible trade balance</i>	2.6

Note 1 Preliminary figures.

7. Annual averages of the unemployment and underemployment rates and growth in labour force and total employment:

	<i>Unemployment rate (%)</i>	<i>Underemployment rate (%)</i>	<i>Growth in labour force (%)</i>	<i>Growth in total employment (%)</i>
2012	3.3	1.5	2.2	2.4
2013	3.4	1.5	1.9	1.8
2014	3.2	1.5	0.7	0.9

8. Annual rates of change in the Consumer Price Indices:

	<i>Composite CPI</i>		<i>CPI(A)</i>	<i>CPI(B)</i>	<i>CPI(C)</i>
	<i>Headline (%)</i>	<i>Underlying (%)</i>	<i>(%)</i>	<i>(%)</i>	<i>(%)</i>
2012	4.1	4.7	3.6	4.3	4.1
2013	4.3	4.0	5.1	4.1	3.8
2014	4.4	3.5	5.6	4.2	3.5

ECONOMIC PROSPECTS FOR 2015

Forecast rates of change in the Gross Domestic Product and prices in 2015:

	(%)
Gross Domestic Product (GDP)	
<i>Real GDP</i>	1 to 3
<i>Nominal GDP</i>	2.5 to 4.5
<i>Per capita GDP in real terms</i>	0.2 to 2.1
<i>Per capita GDP at current market prices</i>	HK\$315,200-321,400 (US\$40,400-41,200)
Composite Consumer Price Index	
<i>Headline Composite Consumer Price Index</i>	3.5
<i>Underlying Composite Consumer Price Index</i>	3
GDP Deflator	1.5
Government Consumption Expenditure Deflator	4