

Press Release

(embargoed until 4:30 p.m. on 11 August 2017)

Economic Situation in the Second Quarter of 2017 and Latest GDP and Price Forecasts for 2017

The Government released today (11 August) the Half-yearly Economic Report 2017, together with the preliminary figures on Gross Domestic Product (GDP) for the second quarter of 2017.

Deputy Government Economist, Mr Andrew Au, described the economic situation in the second quarter of 2017 and provided the latest GDP and price forecasts for 2017.

Main points

- * The Hong Kong economy sustained above-trend growth in the second quarter of 2017, expanding by 3.8% in real terms over a year earlier, following notable growth of 4.3% in the first quarter. The generally benign global economic environment remained supportive to external demand. Domestic demand growth stayed robust, buttressed by favourable labour market conditions and improved economic sentiment. On a seasonally adjusted quarter-to-quarter comparison, real GDP picked up to grow by 1.0% in the second quarter, following 0.7% growth in the preceding quarter.
- * External demand improved further in the second quarter, with downside risks to the global economic outlook receding. This continued to render support to Asia's regional trading and manufacturing activities. Against this backdrop, Hong Kong's total exports of goods registered visible year-on-year growth of 5.6% in real terms in the second quarter, with exports to Asian markets providing the main growth impetus. Meanwhile, exports of services grew at a steady pace of 2.3% year-on-year in real terms amid reviving regional trade flows and increased cross-border financial activities, notwithstanding the stuttered recovery in inbound tourism.
- * The domestic sector continued to display strength. Private consumption expenditure grew briskly by 5.3% in real terms in the second quarter over a year earlier, underpinned by favourable labour market conditions and stronger wealth effects. Meanwhile, overall investment expenditure strengthened to show sizeable growth of 8.0% year-on-year in real terms, as machinery and equipment acquisition rebounded and building and construction activity sustained its uptrend.
- * The labour market tightened along with the above-trend pace of economic expansion. Total employment saw further sturdy growth in the second quarter, and the seasonally adjusted unemployment rate went down slightly to 3.1%, the lowest level in more than three years. Wages and earnings improved further in real terms.

- * The rally in the local stock market at the beginning of this year extended well into recent months. Market sentiment was rather bullish amid the improved global economic outlook, driving up many major overseas stock markets. The residential property market stayed largely active during the second quarter, though the pace of price gains slowed somewhat over the course of the quarter.
- * Looking ahead, the global economy is on course to attain further moderate expansion in the rest of the year, as the more prominent downside risks to the outlook have been receding. Major advanced economies are likely to continue to improve. The growth momentum of the Mainland economy has also been stronger than earlier expected. These developments should be conducive to the near-term performance of Asia's and Hong Kong's exports. However, there is still a need to stay alert to the uncertainties in the external environment, including the pace of US monetary policy normalisation, policy differences among major central banks and Brexit-related negotiations. Besides, a possible rise in protectionist sentiment and heightened geopolitical tensions in various regions also warrant attention.
- * Domestic demand should remain firm. Favourable employment and income conditions will continue to bode well for private consumption, while improved economic outlook should lend support to business investment. The continued expansion in building and construction activities will also add to the resilience of domestic demand.
- * In view of the likely positive developments on both external and domestic fronts, the Hong Kong economy is expected to attain further solid growth in the rest of the year. Taking into account the stronger-than-expected actual growth outturn of 4.0% in the first half of the year and receding downside risks in the external environment, the real GDP growth forecast for 2017 as a whole is revised upwards to 3-4% in the current round of review, from that of 2-3% in the May round.
- * Inflation pressure has remained moderate. The underlying inflation rate was 2.0% in the second quarter, averaging 1.7% in the first half of the year. The upside risks to consumer price inflation should remain contained in the near term, as global inflation is likely to stay modest and increases in local costs should continue to be moderate. Considering that the actual inflation outturns so far this year have been somewhat lower than expected, the forecast rates of underlying and headline consumer price inflation for 2017 as a whole, at 2% and 1.8% respectively in the May round, are revised slightly downwards in the current round of review, to 1.8% and 1.6% respectively.

Details

GDP

According to the preliminary data on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, GDP grew by 3.8% in real terms in the second quarter of 2017 over a year earlier, following notable growth of 4.3% in the preceding quarter (the same as the preliminary estimate). Both were stronger than the trend growth of 2.9% per annum over the past ten years. For the first half of 2017 as a whole, real GDP expanded by 4.0% year-on-year, doubling its 2.0% growth pace in 2016. On a seasonally adjusted quarter-to-quarter comparison, real GDP picked up to grow by 1.0% in the second quarter, following 0.7% growth in the preceding quarter (the same as the preliminary estimate) and representing the fifth consecutive quarter of expansion (*Chart*).

2. The latest figures on GDP and its major expenditure components up to the second quarter of 2017 are presented in *Table 1*. Developments in different segments of the economy in the second quarter of 2017 are described below.

External trade

3. *Total exports of goods* grew visibly by 5.6% in real terms in the second quarter over a year earlier, following marked growth of 9.3% in the preceding quarter when there was a fall-off in external demand a year ago. Among major markets, with reference to external merchandise trade statistics, exports to Asian economies remained the key growth driver of our overall exports in the second quarter, as the demand for raw materials, semi-manufactures and capital goods remained robust amid reviving regional trading and manufacturing activities. Specifically, exports to the Mainland sustained solid growth, and those to some emerging Asian economies such as India and Vietnam increased strongly. Exports to Japan also picked up to double-digit growth in the second quarter, thanks to recovery in production activities and relative improvement in consumer sentiment there. In contrast, the US and EU markets rose at a modest pace by comparison. On a seasonally adjusted quarter-to-quarter basis, total exports of goods fell by 0.8% in real terms in the second quarter, after notable growth of 1.6% in the first quarter.

4. *Exports of services* grew steadily by 2.3% year-on-year in real terms in the second quarter, after 2.8% growth in the preceding quarter, underpinned by the generally positive global economic environment. Exports of transport services expanded notably, thanks to growth in regional trade and cargo flows. Exports of financial services sustained moderate growth amid increased cross-border financial activities. Exports of business and other services also increased marginally. Meanwhile, exports of travel services fell slightly. The relative improvement that was seen in these exports in recent quarters stuttered, as tourist spending still lacked growth and the recovery in visitor arrivals was unsteady in the second quarter. On a seasonally adjusted quarter-to-quarter basis, exports of services were down by 1.3% in real terms in the second quarter, after growing by 0.6% in the preceding quarter.

Domestic sector

5. The domestic sector continued to display strength. *Private consumption expenditure* grew briskly by 5.3% in real terms in the second quarter over a year earlier, picking up from 3.9% growth in the first quarter. The faster growth in the second quarter mainly reflected robust local consumption demand, which was underpinned by favourable labour market conditions and stronger wealth effects. Also relevant was sizeable year-on-year growth in residents' expenditure abroad, partly helped by the difference in timing of the Easter holidays in 2016 and 2017, which fell in late March last year but mid-April this year. On a seasonally adjusted quarter-to-quarter comparison, private consumption expenditure rose further by 2.0% in real terms in the second quarter. *Government consumption expenditure* maintained steady year-on-year growth of 3.2% in real terms in the second quarter, compared to its 3.1% growth in the preceding quarter.

6. Overall investment spending in terms of *gross domestic fixed capital formation* strengthened to show sizeable growth of 8.0% in real terms in the second quarter over a year earlier, after visible growth of 5.9% in the preceding quarter. Within this, overall building and construction expenditure maintained its uptrend, expanding by 4.0% year-on-year in real terms, as private sector building and construction activity saw further notable growth in the second quarter and public sector building and construction expenditure stayed at a high level. Costs of ownership transfer also increased markedly against a low base of comparison last year. Machinery and equipment acquisition rebounded by 4.6% year-on-year in real terms in the second quarter, after falling for two consecutive quarters.

The labour sector

7. Overall labour market conditions remained favourable and tightened somewhat, with the *seasonally adjusted unemployment rate* going down slightly to 3.1% in the second quarter, the lowest level in more than three years. The *underemployment rate* held steady at 1.2% in the same quarter. Total employment sustained sturdy year-on-year growth in the second quarter. Wages and earnings improved further in real terms. Partly benefitting from the upward adjustment of the Statutory Minimum Wage rate since May 2017, the average monthly employment earnings of full-time employees (excluding foreign domestic helpers) engaged in elementary occupations continued to increase, up by 3.4% year-on-year in real terms in the second quarter.

The asset markets

8. The *local stock market* sustained a general uptrend in the second quarter, similar to the gains in many overseas stock markets. Such favourable developments largely reflected upbeat investor sentiment amid a benign global economic outlook, notwithstanding the uncertainties surrounding the future pace of monetary policy normalisation among major central banks and the complications in Brexit negotiations after the UK general election. The Hang Seng Index closed the second quarter at 25 765, up by 6.9% from three months earlier. The rally in the Hang Seng Index has continued of late, closing at 27 444 on 10 August.

9. The *residential property market* stayed largely active in the second quarter. Trading activities picked up, with the number of residential property transactions increasing from 13 221 in the first quarter to 18 892 in the second quarter. Nevertheless, the number of transactions fell notably to 3 515 in July. Residential property prices rose by 5% between March and June, though the pace of price gains slowed somewhat over the course of the quarter. Compared to the 1997 peak, overall flat prices in June were 94% higher. Moreover, the housing affordability ratio worsened to around 67% in the second quarter. During the second quarter, flat rentals went up by 3%, while shop and office rentals rose by 2% and 1% respectively. To strengthen banks' risk management and resilience, the Hong Kong Monetary Authority in mid-May introduced the eighth round of macro-prudential measures for property mortgage loans.

Prices

10. Consumer price inflation remained moderate in the second quarter. External price pressure was muted, thanks to low inflation in our major import partners. Locally, increases in labour costs stayed largely moderate. Slower rises in fresh-letting residential and commercial rentals in 2016 continued to feed through into the Composite Consumer Price Index, notwithstanding the more visible pick-ups in fresh-letting residential rentals in recent months. Yet, as the temporary effect from the high base of comparison due to the weather-induced spikes in food prices in the early months last year dissipated, consumer price inflation returned to levels that were more in line with the prevailing moderate price pressures in the economy. In sum, netting out the effects of the Government's one-off relief measures to more accurately reflect the underlying inflation trend, *underlying consumer price inflation* was 2.0% in the second quarter, up from 1.4% in the first quarter. Meanwhile, *headline consumer price inflation* also ticked up to 2.0% from 0.5%. Headline consumer price inflation showed a larger up-tick in the second quarter, as the dampening effect of the rates concession on the headline rate in the first quarter largely dissipated.

Latest GDP and price forecasts for 2017

11. Looking ahead, the global economy is on course to attain further moderate expansion in the rest of the year, as the more prominent downside risks to the outlook have been receding. Major advanced economies are likely to continue to improve. The growth momentum of the Mainland economy has also been stronger than earlier expected. These developments should be conducive to the near-term performance of Asia's and Hong Kong's exports. However, there is still a need to stay alert to the uncertainties in the external environment, including the pace of US monetary policy normalisation, policy differences among major central banks and Brexit-related negotiations. Besides, a possible rise in protectionist sentiment and heightened geopolitical tensions in various regions also warrant attention.

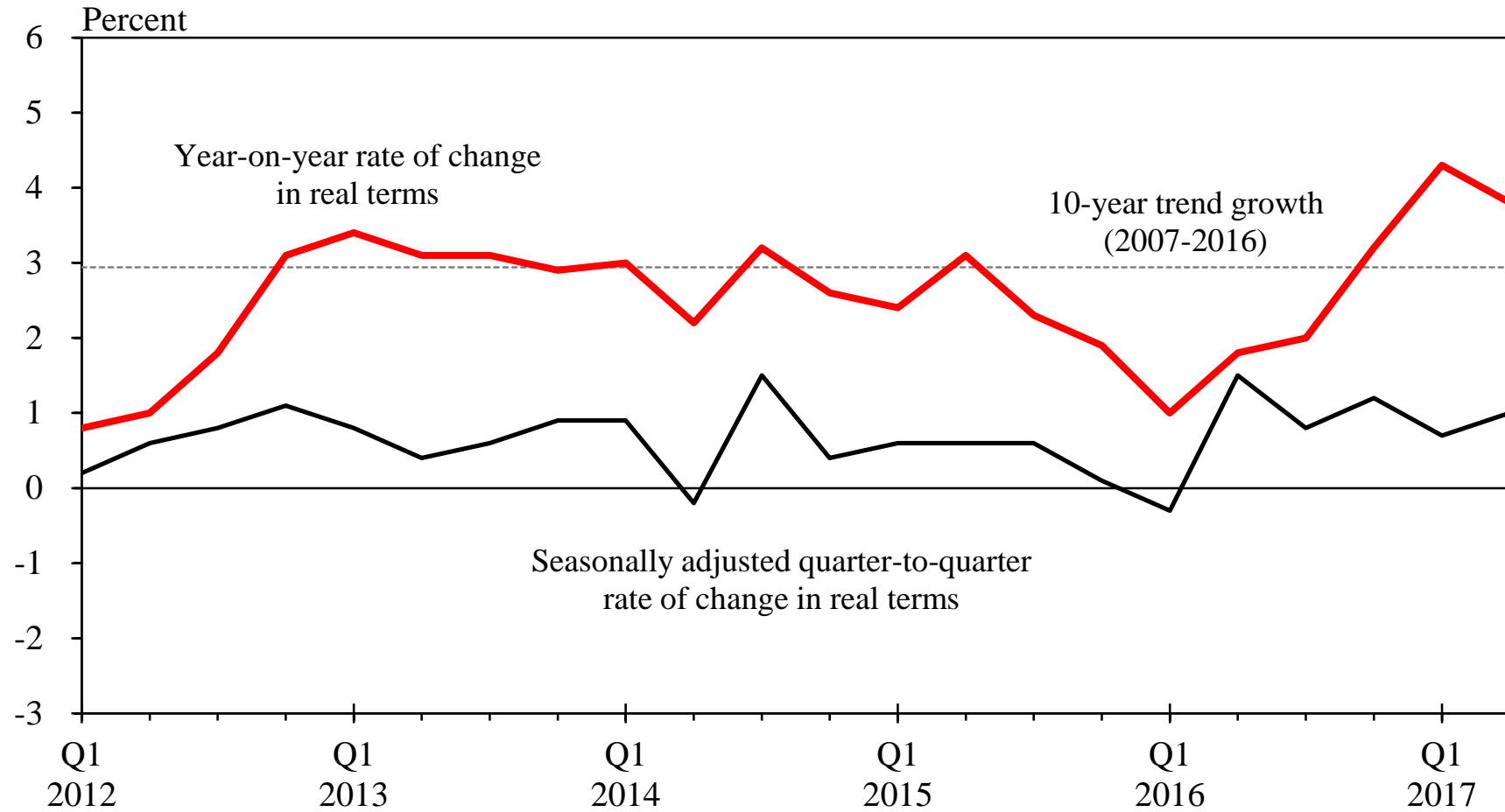
12. Domestic demand should remain firm. Favourable employment and income conditions will continue to bode well for private consumption, while improved economic outlook should lend support to business investment. The continued expansion in building and construction activities will also add to the resilience of domestic demand.

13. In view of the likely positive developments on both external and domestic fronts, the Hong Kong economy is expected to attain further solid growth in the rest of the year. Taking into account the stronger-than-expected actual growth outturn of 4.0% in the first half of the year and receding downside risks in the external environment, the real GDP growth forecast for 2017 as a whole is revised upwards to 3-4% in the current round of review, from that of 2-3% in the May round (*Table 2*). For reference, the latest forecasts by private sector analysts mostly range from 2.1-3.6%, averaging around 2.7%.

14. On inflation outlook, the upside risks to consumer price inflation should remain contained in the near term, as global inflation is likely to stay modest and increases in local costs should continue to be moderate. Considering that the actual inflation outturns so far this year have been somewhat lower than expected, the forecast rates of underlying and headline consumer price inflation for 2017 as a whole, at 2% and 1.8% respectively in the May round, are revised slightly downwards in the current round of review, to 1.8% and 1.6% respectively (*Table 2*).

(The Half-yearly Economic Report 2017 is now available for online download, free of charge at www.hkeconomy.gov.hk/en/reports/index.htm. The Report of the Gross Domestic Product, Second Quarter 2017, which contains the GDP figures up to the second quarter of 2017, is also available for online download, free of charge at the homepage of the Census and Statistics Department, www.censtatd.gov.hk.)

Hong Kong's Gross Domestic Product



Note : Figures for the second quarter of 2017 are preliminary estimates.

Table 1

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

	<u>2015</u> [#]	<u>2016</u> [#]	<u>Q1</u> [#]	<u>Q2</u> [#]	<u>2016</u> <u>Q3</u> [#]	<u>Q4</u> [#]	<u>Q1</u> [#]	<u>2017</u> <u>Q2</u> ⁺
<i>Change in real terms of GDP and its main expenditure components (%)</i>								
Private consumption expenditure	4.8	1.8	1.5 (0.2)	0.4 (0.7)	1.6 (1.1)	3.6 (1.5)	3.9 (0.5)	5.3 (2.0)
Government consumption expenditure	3.4	3.4	3.2 (0.9)	3.6 (1.0)	3.4 (0.5)	3.4 (0.9)	3.1 (0.6)	3.2 (1.1)
Gross domestic fixed capital formation	-3.2	-0.3	-8.7	-5.1	7.2	5.6	5.9	8.0
Building and construction	2.2	3.9	1.5	2.4	4.3	7.5	8.6	4.0
Costs of ownership transfer	-8.3	-2.9	-50.9	-19.2	22.5	63.7	77.3	53.4
Machinery, equipment and intellectual property products	-7.7	-4.6	-10.8	-10.3	7.6	-4.2	-8.6	4.6
Total exports of goods ^{&}	-1.7	1.8	-3.5 (-2.5)	2.4 (3.0)	2.5 (0.7)	5.1 (3.9)	9.3 (1.6)	5.6 (-0.8)
Imports of goods ^{&}	-2.7	1.1	-5.6 (-3.8)	0.6 (3.6)	3.1 (1.9)	5.6 (4.0)	10.0 (0.3)	6.2 (-0.2)
Exports of services ^{&}	0.3	-3.2	-5.4 (-1.0)	-6.2 (-0.6)	-2.5 (1.8)	1.2 (1.1)	2.8 (0.6)	2.3 (-1.3)
Imports of services ^{&}	5.0	2.0	4.1 (1.7)	1.2 (-1.1)	0.8 (-0.2)	2.0 (1.6)	0.9 (0.5)	3.5 (1.6)
Gross Domestic Product	2.4	2.0	1.0 (-0.3)	1.8 (1.5)	2.0 (0.8)	3.2 (1.2)	4.3 (0.7)	3.8 (1.0)
<i>Change in the main price indicators (%)</i>								
GDP deflator	3.6	1.8	2.1 (0.5)	1.7 (0.5)	1.5 (0.2)	1.8 (0.6)	2.1 (0.8)	3.1 (1.4)
Composite CPI								
Headline	3.0 [@]	2.4	2.8 (0.7)	2.6 (-0.6)	3.1 (0.4)	1.2 (0.7)	0.5 (0.1)	2.0 (0.7)
Underlying [^]	2.5 [@]	2.3	2.8 (0.7)	2.3 (0.2)	2.1 (0.5)	2.1 (0.7)	1.4 (0.1)	2.0 (0.7)
<i>Change in nominal GDP (%)</i>	6.1	3.9	3.2	3.6	3.6	5.0	6.5	7.0

Notes : Figures are subject to revision later on as more data become available. The 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 this category due to the presence of considerable short term fluctuations.

(&) Figures are compiled based on the change of ownership principle in recording goods sent abroad for processing and merchanting under the standards stipulated in the *System of National Accounts 2008*.

(#) Revised figures.

(+) Preliminary figures.

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

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

(@) The year-on-year rates of change of the CPIs from the fourth quarter of 2015 onwards are computed from the new 2014/15-based series, and those before are from the old 2009/10-based series. Splicing has been applied to the indices in order to obtain better estimates of the rates of change for the year 2015.

Table 2**Economic forecasts for 2017
(rate of change (%))**

	Forecasts as released on <u>12.5.2017</u> (%)	Latest forecasts on <u>11.8.2017</u> (%)
Real Gross Domestic Product (GDP)	2 to 3	<i>3 to 4</i>
Composite Consumer Price Index (CCPI)		
<i>Underlying CCPI</i>	2	<i>1.8</i>
<i>Headline CCPI</i>	1.8	<i>1.6</i>