



2007 Economic Background and 2008 Prospects

Government of the Hong Kong
Special Administrative Region

***2007 ECONOMIC BACKGROUND
AND
2008 PROSPECTS***

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CALENDAR OF EVENTS OF SIGNIFICANCE FOR THE HONG KONG ECONOMY IN 2007

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CHAPTER 1 : OVERVIEW OF ECONOMIC PERFORMANCE IN 2007

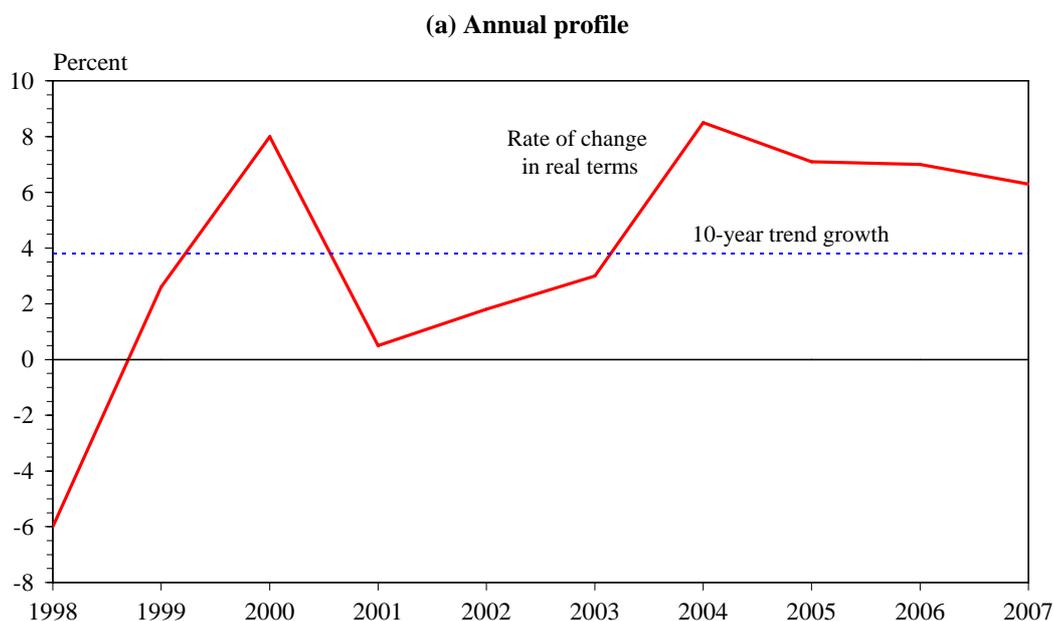
Summary

- *The Hong Kong economy sustained a robust growth momentum throughout 2007, with GDP leaping by 6.3% in real terms. This followed a 7.0% growth in 2006 (figure revised up from 6.8%) and marked the fourth consecutive year of strong economic expansion. The economy had been resilient to the global financial market turbulence. High value-added sectors, such as financial services, and trading and logistics, were again amongst the out-performers as the economy moves up the value chain.*
- *The external sector performed rather well in spite of the weakening import demand from advanced economies, thanks largely to vibrant trade flows to and from the Mainland and a superb growth in exports of services. Amidst upbeat consumer and business sentiments, domestic demand has become an increasingly important contributor to overall economic growth.*
- *The labour market improved notably further in 2007, with unemployment rate falling to 3.4% by year-end. The strong labour demand pushed vacancies to the highest since 1997, allowing workers at different skill levels to benefit from the economic upturn. The tightened labour market also pushed up wages and earnings.*
- *The financial sector continued to benefit from the on-going integration with the Mainland. Stock prices and market turnover surged to record highs in October 2007, before concerns about global financial market turbulence caused some pull-back. The property market improved distinctly further, particularly in the latter part of 2007, with a marked pick up in both sale prices and transactions under a favourable interest rate environment and the persistent strength in the economy.*
- *Inflationary pressures trended upward in 2007, amidst the strong economic upturn and global food and energy inflation. Although improvement in labour productivity offered some alleviating effects, external price pressures from rising food and energy prices and weakening of Hong Kong dollar alongside the slide in US dollar became increasingly visible over the course of the year.*

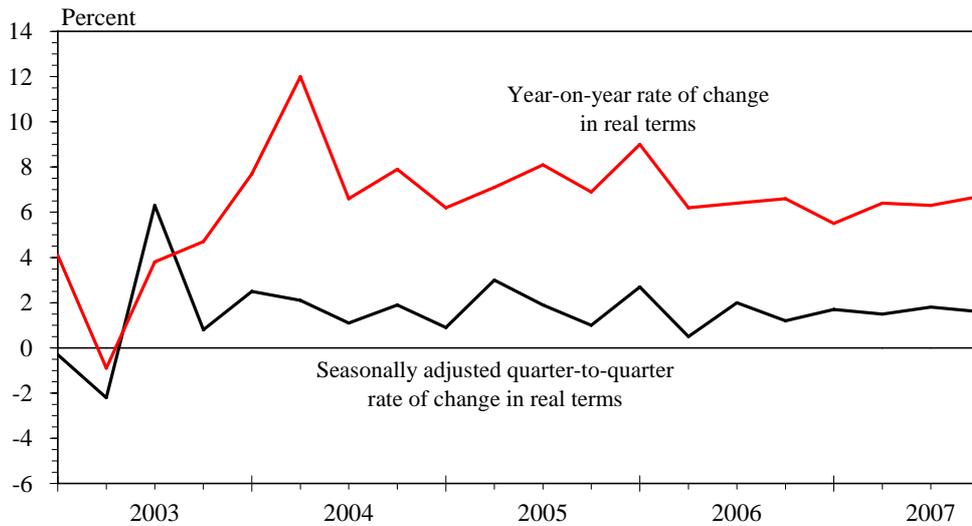
Overall situation

1.1 The Hong Kong economy showed another year of vibrant performance in 2007. Economic growth was at over 6% in each of the past four years. The last four-year period of comparable performance was 1978-1981. The economy had been resilient to the global financial market turbulence, with both the external and domestic sectors holding up well in 2007. Overall exports attained further notable growth. Consumption demand was strong amidst rising income, buoyant labour market, and better asset market performance. Investor sentiment was also upbeat, in face of the ample business opportunities emanating from the economy's integration with the fast-growing Mainland economy. Against this background, the labour market improved distinctly over the course of the year with unemployment rate falling to the lowest level in almost ten years. Meanwhile, the sustained economic upturn and global food and energy inflation led to stronger inflationary pressures.

Diagram 1.1 : The economy registering another year of above-trend growth



(b) Quarterly profile



1.2 For 2007 as a whole, the *Gross Domestic Product (GDP)*⁽¹⁾ jumped by 6.3% in real terms, following the strong 7.0% growth in 2006 (figure revised up from 6.8%). On a year-on-year comparison, economic growth was above trend throughout the four quarters of 2007, picking up from 5.5% in the first quarter to 6.4% in the second quarter and 6.3% in the third quarter, and further to 6.7% in the fourth quarter. The strengthening domestic demand helped to sustain GDP growth at a stronger pace in the latter part of the year. On a seasonally adjusted quarter-to-quarter comparison⁽²⁾, GDP expanded strongly during the year, by 1.7%, 1.5%, 1.8% and 1.6% respectively in the four quarters.

**Table 1.1 : Gross Domestic Product and its main expenditure components
and the main price indicators
(year-on-year rate of change (%))**

	<u>2006[#]</u>	<u>2007⁺</u>	<u>2006</u>				<u>2007</u>			
			<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4⁺</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>										
Private consumption expenditure	6.0	7.8	6.1 (2.4)	7.2 (1.3)	4.6 (0.1)	6.1 (1.8)	4.5 (1.4)	5.8 (2.7)	10.6 (3.7)	10.0 (2.0)
Government consumption expenditure	0.1	2.3	1.4 (1.6)	-1.5 (-1.3)	-0.9 (0.8)	1.3 (0.9)	2.3 (1.6)	2.9 (-0.3)	1.5 (-0.3)	2.3 (1.2)
Gross domestic fixed capital formation	7.0	6.0	6.4	4.0	10.0	7.5	2.8	10.0	1.0	10.4
<i>of which :</i>										
Building and construction	-7.3	0.2	-11.6	-3.1	-10.2	-3.7	-2.2	6.5	-0.9	-2.3
Machinery, equipment and computer software	19.1	6.6	25.1	13.5	23.8	14.9	3.6	11.2	-0.4	11.9
Total exports of goods	9.3	7.2	13.7 (3.2)	5.5 (0.1)	7.9 (4.2)	10.6 (2.3)	6.6 (0.4)	10.1 (2.9)	6.4 (0.3)	5.9 (1.8)
Imports of goods	9.2	9.0	13.3 (2.5)	6.0 (0.4)	7.5 (3.9)	10.6 (3.1)	7.1 (0.1)	11.6 (4.2)	8.3 (0.7)	8.8 (3.2)
Exports of services	10.1	11.2	10.9 (2.1)	11.0 (2.4)	9.3 (2.0)	9.3 (2.8)	10.0 (2.7)	11.6 (3.2)	12.6 (3.4)	10.5 (1.0)
Imports of services	8.1	8.1	5.6 (2.4)	11.2 (4.4)	6.8 (-0.3)	9.0 (2.2)	5.7 (-0.2)	8.0 (5.9)	9.1 (1.1)	9.1 (2.1)
Gross Domestic Product	7.0	6.3	9.0 (2.7)	6.2 (0.5)	6.4 (2.0)	6.6 (1.2)	5.5 (1.7)	6.4 (1.5)	6.3 (1.8)	6.7 (1.6)
<i>Change in the main price indicators (%)</i>										
GDP deflator	-0.3	2.8	-0.3 (-0.3)	-0.3 (0.1)	-1.0 (*)	0.6 (0.7)	1.2 (0.5)	1.8 (0.9)	3.3 (1.3)	4.7 (1.9)
Composite Consumer Price Index	2.0	2.0	1.6 (0.4)	2.0 (0.8)	2.3 (0.5)	2.1 (0.4)	1.7 (*)	1.3 (0.3)	1.6 (0.8)	3.5 (2.2)
<u>Change in nominal GDP (%)</u>	6.7	9.3	8.7	5.8	5.4	7.2	6.8	8.3	9.8	11.7

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.

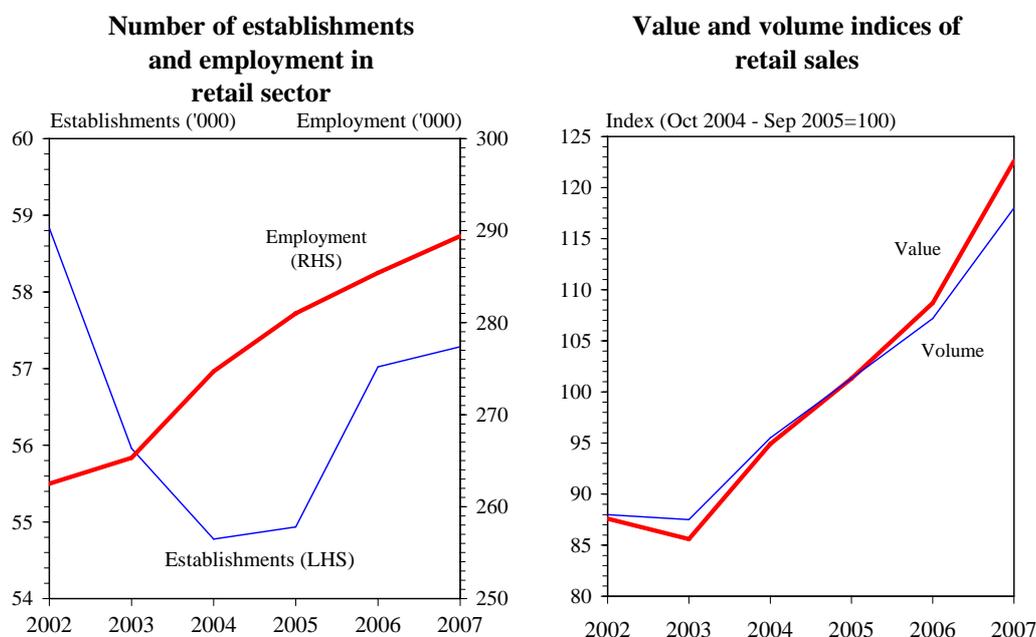
(*) Change of less than 0.05%.

Box 1.1

Recent developments in retail business and the contribution from inbound tourism

The retail sector is one of the largest service industries, in terms of number of establishments and employed persons, in Hong Kong. In 2007, the number of establishments in the retail trade industry was about 57 000, employing some 289 000 persons or about 8.3% of Hong Kong's total employment. In terms of economic contribution, the retail trade directly generated \$37.6 billion of value added in 2006 (latest available figure), equivalent to 2.6% of the GDP of Hong Kong.

The retail trade industry went through a period of consolidation in 2003 due to the outbreak of the Severe Acute Respiratory Syndrome, but has recovered progressively along with the economic upturn over the past few years. The number of employment in the retail industry increased steadily since 2003, at an average annual rate of 2.2%, to 289 000 in the first three quarters of 2007. Given the relatively labour-intensive nature of retail business, it is an important source of employment for the local workforce.

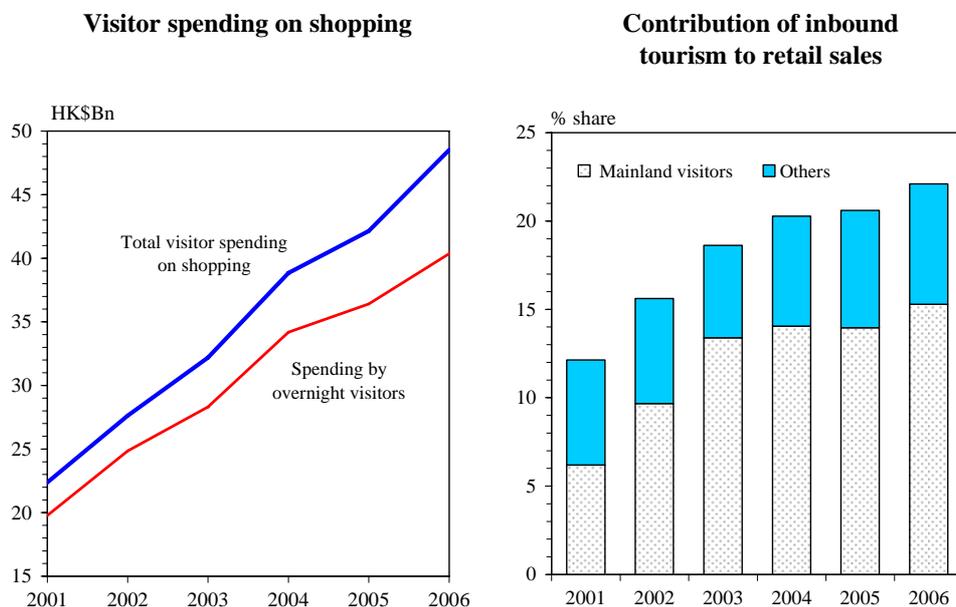


Retail business grew notably over the past several years reaching \$247.7 billion in 2007, achieving an annual average growth rate of 9.4% in value terms or 7.8% in volume terms during 2003 to 2007. Apart from the economic recovery, the vibrant inbound tourism, particularly after the launch of the Individual Visit Scheme in July 2003, has also been an important force driving the performance of retail business.

Being one of the most popular destinations for Mainland visitors and also visitors from the Asia Pacific region, Hong Kong saw its total number of visitors surpassed 28 million in 2007, substantially up from the figure of 16.6 million in 2002. Reflecting the importance of the Mainland market to Hong Kong's inbound tourism, Mainland visitors accounted for 55% of total visitor arrivals in 2007.

Box 1.1 (Cont'd)

The importance of inbound tourism to retail trade is reflected by the expenditure on shopping of incoming visitors, which amounted to \$48.5 billion in 2006 (the latest available figure). The share of expenditure on shopping of incoming visitors in the total value of retail sales increased distinctly from 15.6% in 2002 to a share of 22.1% in 2006.



Specifically, expenditure on shopping by Mainland visitors increased substantially from \$17.1 billion in 2002 to \$33.6 billion in 2006, at an average annual rate of 18.4%. The share of such expenditure in Hong Kong's total retail sales value rose from 9.7% in 2002 to 15.3% in 2006. Analysed by shopping categories, "jewellery and watches" and "clothing" had been the two largest categories that the Mainland visitors spent on, each of which accounted for about a quarter of their total spending on shopping in 2006.

Over the past two years or so, there has also been a significant improvement in confidence among the local consumers. This has also contributed markedly to the recent impressive performance of retail sales. Private consumption expenditure, which is actually a better gauge of consumption spending by local residents on account of its broader coverage and its exclusion of visitor spending, rose markedly by 7.8% in real terms in 2007, the fastest increase since 1993. The improving job security, rising income, better household financial positions and stronger performance of asset markets have all help underpin the upbeat sentiments among the local consumers.

The near-term prospects for the retail business remain promising. Inbound tourism is likely to continue to benefit from the thriving Mainland economy and fairly robust growth momentum in other Asian economies. The prevailing strong consumer confidence should also bode well for retail sales in 2008.

The external sector

1.3 The external sector on the whole continued to display strength in 2007. Merchandise exports showed a notable growth in 2007, although the growth pace moderated somewhat in the second half of the year. Although the US and Japan markets were weak, it was compensated by the strong growth in the Mainland and many other emerging Asian markets. The weaker Hong Kong dollar along with the global weakness of the US dollar also contributed positively to the price competitiveness of Hong Kong's exports. For 2007 as a whole, *total exports of goods* rose by 7.2% in real terms, compared with the 9.3% increase in 2006.

1.4 Service trade continued to be a bright spot in the economy, with growth buoyed considerably by hectic financial market activity, vibrant inbound tourism (especially in the second half) and continued demand for merchanting and other trade-related services (mainly offshore trade). Exports of transportation services, on the other hand, rose at a relatively moderate pace. Overall, *exports of services* surged by 11.2% in 2007, accelerating from the 10.1% gain in 2006. The persistently stellar demand for Hong Kong's services is a testament to the city's status as a regional hub for business, financial, trade and travel services.

The domestic sector

1.5 Domestic demand is progressively becoming a more important growth engine for the economy. Local consumption demand grew robustly in 2007, particularly evident in the second half of the year, on the back of rising income, a robust labour market and strong performance of the asset markets. *Private consumption expenditure (PCE)* grew by 7.8% in real terms for 2007 as a whole, up from the 6.0% growth in 2006. This was also the fastest growth since 1993. Demand was especially strong in consumer goods and services.

**Table 1.2 : Consumer spending by major components^(a)
(year-on-year rate of change in real terms (%))**

		Total consumer spending in the domestic market ^(a)	<i>Of which :</i>					Residents' expenditure abroad	Visitor spending	Private consumption expenditure ^(b)
			Food	Durables	Non- durables	Services				
2006	Annual	6.1	3.8	9.5	6.5	6.0	5.0	6.4	6.0	
	Q1	6.9	5.1	7.5	6.4	7.3	1.7	8.8	6.1	
	Q2	6.7	4.3	7.6	6.2	7.2	11.6	6.0	7.2	
	Q3	5.1	2.1	10.3	6.9	4.2	0.6	4.6	4.6	
	Q4	5.9	3.9	12.1	6.4	5.2	7.3	6.3	6.1	
2007	Annual	8.7	1.6	19.0	10.8	7.7	3.8	13.3	7.8	
	Q1	5.3	2.4	10.3	7.4	4.3	3.0	10.8	4.5	
	Q2	6.4	1.7	16.2	7.3	5.6	3.6	10.3	5.8	
	Q3	11.5	3.5	25.6	12.5	10.4	5.5	14.7	10.6	
	Q4	11.4	-0.8	23.2	15.3	10.5	3.0	16.8	10.0	

Notes : (a) Consumer spending in the domestic market comprises both local consumer and visitor spending, which are not separable from the survey data.

(b) Private consumption expenditure is obtained by deducting visitor spending from the total consumer spending in the domestic market, and adding back residents' expenditure abroad.

1.6 The growth rate of overall investment remained firm at 6.0% in 2007. Investment in machinery, equipment and software registered a notable 6.6% growth in 2007, though less rapid than the blistering double-digit pace in the previous three years. Construction activities began to show some signs of stabilising in 2007, thanks largely to the rebound in private sector activities when their public sector counterparts remained lacklustre. According to the Quarterly Business Tendency Survey conducted by the Census and Statistics Department during mid-December 2007 to mid-January 2008, business confidence as revealed by the large establishments in different sectors still generally held up well.

Diagram 1.2 : Consumer spending gathered strong momentum

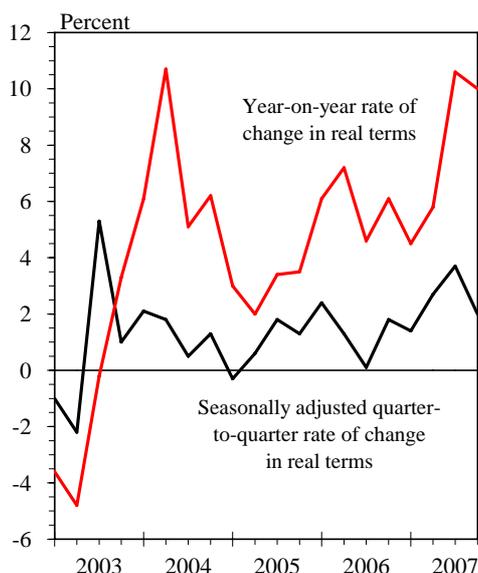
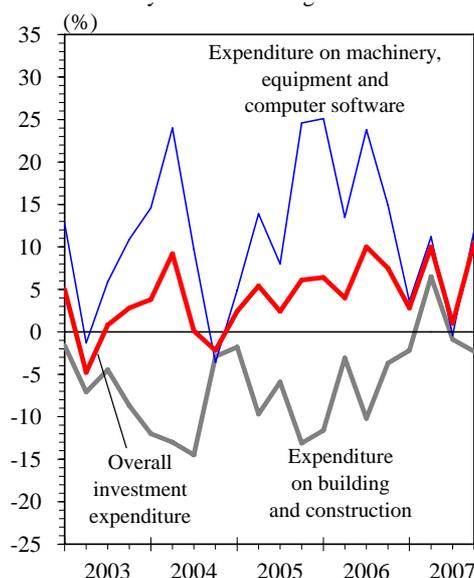


Diagram 1.3 : Overall investment continued to rise



The labour sector

1.7 The labour market improved distinctly further amidst the sustained economic expansion. *Total employment* increased by 2.5% in 2007, accelerating further from the 2.1% gain in 2006, and the total number of employed persons reached an all-time high of 3.53 million in the fourth quarter of 2007 (and rose further to a new high of 3.55 million in the three months ending January 2008). Since the trough in 2003, a total of 366 300 additional new jobs had been created. In tandem, the *seasonally adjusted unemployment rate* fell to 3.4% in the fourth quarter of 2007, the lowest in almost ten years (and the unemployment rate held steady at this level in the three months ending January 2008).

1.8 The shift of the economy towards higher value-added activities and the buoyant financial markets resulted in sustained strong demand for professional and higher-skilled workers. The unemployment rate at the upper segment of the labour market stayed below the 2%-mark for the most part of 2007. The pick up in domestic demand also provided significantly more opportunities for the lower-skilled workers, cutting their unemployment rate to 3.7% by the end of 2007, down markedly from the peak of 10.1% in mid-2003. The greater availability of employment opportunities also slashed the number of long-term unemployment by about two-thirds from its peak in 2003, suggesting that lower-skilled workers were able to benefit from the current economic upturn as well. In 2007, labour income continued to rise alongside the broad-based and buoyant labour demand.

The asset markets

1.9 The *residential property market* was firmly supported by the improving household income and financial positions amidst the brisk economic expansion in 2007. The favourable interest rate environment in the second half of the year was another catalyst for demand. By December 2007, flat prices were around 24% higher than a year ago while rentals increased by 15% over a year earlier. The number of transactions in residential properties rose markedly, by 50% from the level in 2006. Nevertheless, flat prices at end-2007 were still on average more than 30% below the peak in 1997 and home purchase affordability remained generally strong relative to the situation in the pre-1997 era.

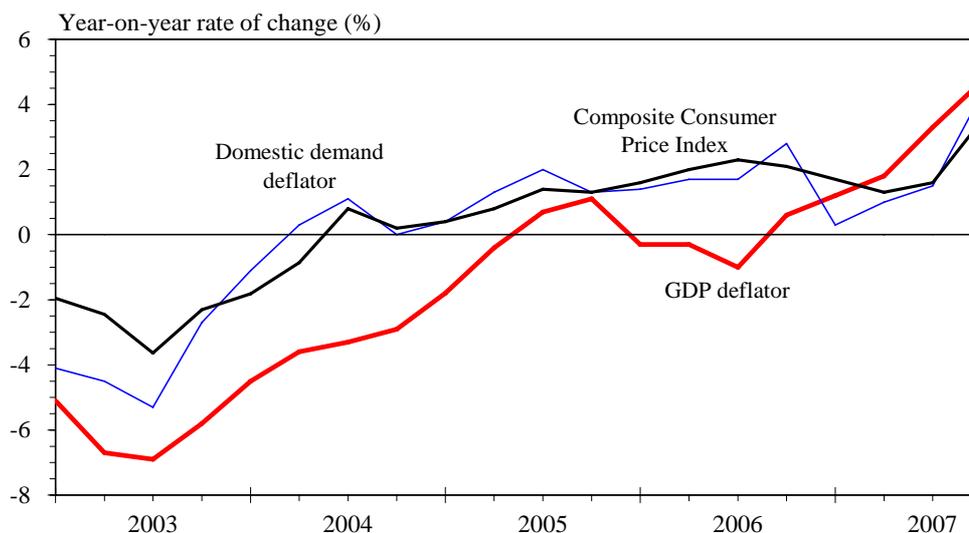
1.10 In the financial market, the *local stock market* followed through on the momentum built in 2006 and staged another sharp rally during most of 2007 amidst the inflow of capital. The Hang Seng Index broke the 30 000 mark for the first time in October. However, the concerns about further global financial market turbulence led to corrections in stock markets around the world since November. The Hang Seng Index closed the year at 27 813, still 39% higher than at end-2006. The average daily turnover and stock market capitalisation swelled further to \$88.1 billion and \$20.7 trillion respectively. Apart from attracting overseas investors to invest into companies operating in the burgeoning Mainland economy, as the 439 Mainland enterprises listed on the Hong Kong stock market accounted for 58% of the total market capitalisation at end-2007, the market is also increasingly serving as a platform for managing the investment of Mainland enterprises and individuals. Backed by upbeat investor sentiment, fund raising activities were robust during most of 2007.

Inflation

1.11 Consumer price inflation climbed up during 2007 alongside the sustained brisk economic expansion. Apart from the external forces such as global food and energy inflation and the weakening of Hong Kong dollar given the drop in US dollar, the strengthened pricing power of retailers because of the buoyant consumption market was another factor that put upward pressure on local prices in spite of the sustained productivity gains. The edging-up of housing cost was another development that should deserve attention. The headline *Composite Consumer Price Index* in 2007 rose by an average of 2.0% over 2006, while the underlying Composite CPI (which nets out effects of public rental waiver in February 2007 and rates concession for the second and third quarters of 2007) for the year as a whole was 2.8% higher than in 2006.

1.12 The *GDP deflator* increased by 2.8% in 2007, bucking its downward trend in the previous eight years. The rise in GDP deflator was attributable partly to the stronger domestic demand pressure and partly to the improvement in terms of trade on the back of a faster increase in export prices. Excluding the effect of terms of trade, the domestic demand deflator rose by 1.9% in 2007.

Diagram 1.4 : Underlying inflation pressures climbing up



GDP by economic activity

1.13 The growth of the services sector continued to outpace that of the overall economy. In terms of net output or value-added, the services sector rose robustly by 7.1% in real terms in the first three quarters of 2007 over a year earlier. Among the constituent service sectors, financing and insurance persistently outperformed other sectors, due to the flourishing local investment markets, while the growth pace of restaurants and hotels, wholesale and retail trades, and import and export trade was also strong. Meanwhile, both the manufacturing and construction sectors recorded modest declines in net output.

**Table 1.3 : GDP by economic activity^(a)
(year-on-year rate of change in real terms (%))**

	<u>2007</u>			<u>2006</u>				<u>2007</u>	
	<u>2006</u>	<u>Q1-Q3</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
Manufacturing	2.2	-2.0	7.0	5.3	-0.6	-1.4	-1.5	-2.3	-2.1
Construction	-9.8	-2.0	-13.8	-5.6	-13.0	-5.8	-6.2	3.7	-2.9
Services ^(b)	7.2	7.1	8.4	6.4	6.6	7.4	6.7	7.1	7.3
Wholesale, retail and import and export trades, restaurants and hotels	8.8	7.3	11.2	6.4	8.9	8.7	6.9	7.5	7.5
Import and export trade	9.0	7.0	12.1	5.7	9.1	9.1	6.7	7.5	6.7
Wholesale and retail trades	7.1	8.3	6.5	6.6	8.4	6.8	6.3	7.7	10.7
Restaurants and hotels	9.4	8.7	9.3	11.2	8.6	8.4	8.7	7.4	10.1
Transport, storage and communications	6.8	5.2	9.4	4.7	6.1	7.2	4.0	4.8	6.7
Transport and storage	6.6	5.2	9.1	4.1	5.8	7.5	3.7	4.4	7.3
Communications	7.7	5.3	10.6	7.3	7.3	5.7	5.7	6.8	3.5
Financing, insurance, real estate and business services	12.2	14.3	12.7	12.7	10.0	13.3	13.8	14.0	15.1
Financing and insurance services	19.7	18.9	21.9	21.2	15.2	20.2	17.6	17.8	21.5
Real estate and business services	2.0	6.9	0.4	0.5	3.1	3.7	7.7	7.3	5.6
Community, social and personal services	1.8	1.3	1.5	1.6	2.0	1.9	1.6	1.4	0.8

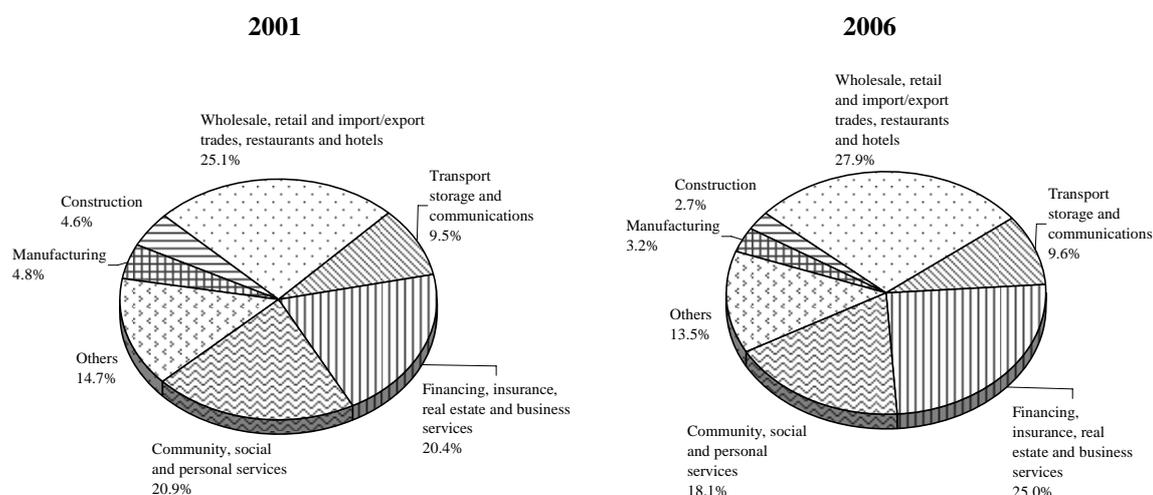
Notes : Figures are subject to revision later on as more data become available.

(a) The GDP figures shown in this table are compiled from the production approach, in parallel with those shown in Table 1.1 which are compiled from the expenditure approach. For details, see Note (1) to this chapter.

(b) In the context of value-added contribution to GDP, the service sectors include ownership of premises as well, which is analytically a service activity.

1.14 Over the past five years, Hong Kong continued to move further towards a service-oriented economy. The on-going restructuring process allows Hong Kong to take advantage of the changing global economic environment as well as to meet the rising demand for high quality services from the Mainland economy and other parts of the world. Between 2001 and 2006, the contribution of the service sectors as a whole to GDP rose from 87.3% to 91.2%, while those of the manufacturing sector and the construction sector fell from 4.8% and 4.6% to 3.2% and 2.7% respectively.

Diagram 1.5 : Economy becoming highly service-oriented



1.15 The Hong Kong economy has been relentlessly putting efforts into restructuring itself into a knowledge-based economy. A quality workforce which is capable of continuously upgrading the level of services remains a vital competitive edge for Hong Kong in face of the keen competition in the global marketplace. For the service sectors as a whole, the share in total employment enlarged from 84.4% in 2002 to 86.6% in the first three quarters of 2007, indicative of the flexibility of labour resources in shifting across sectors. By comparison, the shares of the manufacturing sector and the construction sector shrank from 6.0% and 8.8% respectively to 4.9% and 8.0% over the same period. The transformation has been supported by the increased availability of skilled workers, as the proportion of the workforce attaining tertiary education over the past five years rose further from 26.4% to 30.3%.

Box 1.2

Contribution to economic growth through education and experience upgrading

As discussed in Box 1.2 in the 2007 *Third Quarter Economic Report*, education and experience upgrading have contributed significantly to the accumulation of human capital stock in Hong Kong. This article followed the previous discussion by showing that the continual increase in human capital stock has led to labour productivity growth, and hence economic growth.

Decomposition of sources of labour productivity growth

As a refresher of the analytical framework laid out in the previous article, the construction of the human capital stock series is based on headcount employment adjusted for the age-education specific productivity content or earning potential. This makes tracing the sources of productivity growth possible.

In common usage, labour productivity (LP) is defined as the output of the economy (GDP) divided by employment (EMP):-

$$LP = \frac{GDP}{EMP}$$

In principle, the labour productivity growth can be decomposed into two factors, one being the education upgrading and experience accumulation in the workers employed ($\hat{K}_{EMP} - \hat{EMP}$), the other being the underlying human capital stock productivity increase ($\hat{GDP} - \hat{K}_{EMP}$), which is the component of labour productivity growth due to other factors.

$$LP = \frac{GDP}{EMP} = \frac{GDP}{K_{EMP}} \cdot \frac{K_{EMP}}{EMP}$$
$$\hat{LP} = \underbrace{(\hat{GDP} - \hat{K}_{EMP})}_{\text{Underlying human capital productivity growth}} + \underbrace{(\hat{K}_{EMP} - \hat{EMP})}_{\text{Labour productivity growth from education upgrade and experience accumulation}}$$

where

\hat{LP} = Labour productivity growth

\hat{GDP} = GDP growth

\hat{K}_{EMP} = Growth in human capital stock in employment

\hat{EMP} = Rate of increase in employment

Labour productivity growth from education and experience factors

To facilitate comparison, an alternative human capital stock series is constructed by adjusting headcounts by education-specific income ratios (instead of age-education specific income ratios), so that the gap between this series and the headcount series represents the uplifting effect on productivity due to education upgrading. In addition, using age structure of the population as a proxy for experience accumulation, a third human capital stock series is compiled by using age-specific income ratios, for gauging the separate effect of experience accumulation on productivity.

Box 1.2 (Cont'd)

By applying these decompositions, the contributions to productivity growth from education upgrading and experience accumulation as individual factors are given in the first and second columns of **Table 1** respectively. The combined effects of the two factors are given in the third column. Figures in the brackets represent the part of productivity growth not explained by the specified factors.

Table 1 Productivity gain is much more obvious when taking the effects of education uplifting and experience accumulation together

Productivity lift due to education upgrading and demographics

Year	Education factor		Experience factor		Education & experience combined	
Contribution to trend growth in labour productivity (% point)						
1997 - 2006 (10 years)	1.3	(1.4)	0.3	(2.4)	2.0	(0.8)

Note: Due to rounding, the horizontal addition may not equal to the trend growth in labour productivity over the period.

Considering solely the education upgrading in the population, the factor alone accounted for some 1.3 percentage points of the 2.8% trend growth in labour productivity over the past 10 years. Separately, only 0.3 percentage point of the trend growth in labour productivity was explained by experience accumulation alone over the same period. However, either factor when separately assessed tends to ignore the substantial synergy effect that may arise when a more educated worker can make more gains as his experience grows, be it through the learning-by-doing process or other forms of training and learning. This synergy effect had actually been sizeable, as seen from the difference between the third column and the sum of the first two columns in the table. When the education upgrading and experience accumulation within the employed workers are considered altogether, the part of labour productivity growth attributable to these two quality changes in the workers was a remarkable 2.0% per annum over 1997-2006. That was equivalent to about three quarters of the trend labour productivity growth over the same period, and higher than the 1.6 percentage points, which was the horizontal sum of the two factors when considered separately. As such, *the interaction between education and experience on labour productivity uplifting is multiplicative* - when a worker is more educated, the marginal gain in his productivity as his experience grows is much higher than that of his less-educated peer, as seen from the steeper curve of earning potentials over an average tertiary-educated worker's working life than that of the relatively less-educated counterparts in Box 1.2 in the 2007 Third Quarter Economic Report.

From the above decomposition analysis, it is apparent that the two huge sources that have underpinned the impressive labour productivity growth over the past 10 years are (1) rising proportion of workforce with higher education; and (2) experience accumulation as the workforce mature (median age of Hong Kong's workforce in recent years was around 40, approaching the peak of the life-time earning profile especially for the tertiary education group).

Box 1.2 (Cont'd)

This accumulation in experience and upgrading in educational attainments in the overall labour force in deployment can also be illustrated by **Chart 1**, which compares the employment share distributions across the sub-groups divided by age and educational attainment in 1996 and 2006.

Several observations can be made:

1. The overall share of higher-educated workers, who in general possess higher productivity, has increased as per total employment;
2. the increase in the proportion of higher-educated workers aged 40+, who possess a significantly higher productivity than an average worker and their less-educated counterparts, has been notable; and
3. the workforce overall has become more experienced. While in 1996 the age-groups which dominate the headcounts in employment were those younger than 40-44, the age distribution in 2006 seems to have a more balanced pattern.

Chart 1 Demographic shift and education upgrading factors have been conducive to overall productivity growth, and should remain so in the near future

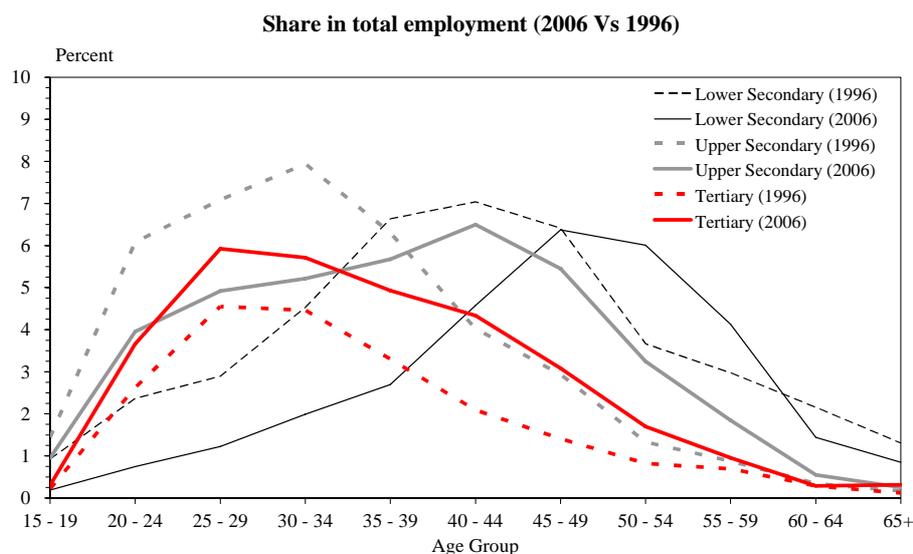


Chart 1 also sheds some light on the labour productivity growth in the near future. With the younger generation in general are more educated than the older ones, *the stream of productivity growth from the process of education uplifting and experience accumulation will go unabated.*

Another important observation from **Table 1** is that after discounting for the play-out of the uplifting effects of education upgrading and experience accumulation, the growth of underlying human capital stock productivity remained sizeable, averaging at 0.8% per annum over the past 10 years. Conventional factors such as technological advancements and intensification of capital stock per capita, while contributing to the realisation in labour productivity growth from education upgrading and experience accumulation in general, should as well be supportive to the underlying productivity growth in this framework. The synergy effect with the Mainland economy may also unlock some of the production capacity previously not seen in the workers.

Box 1.2 (Cont'd)

A comparison is made between Hong Kong's underlying productivity growth and those in the EU economies. The latter figures are extracted from a similar European study on human capital stock. The comparison reflects a relatively strong underlying productivity growth in Hong Kong, as shown in **Table 2**.

Table 2 Growth in Hong Kong's underlying human capital stock productivity compares favourably with the EU economies

**Growth in underlying human capital stock productivity:
HK and selected EU economies (% per annum)**

Hong Kong

1997 - 2006 (10 years) 0.8

EU economies (1993 - 2005)*

Sweden 0.0

United Kingdom -0.1

Finland -0.3

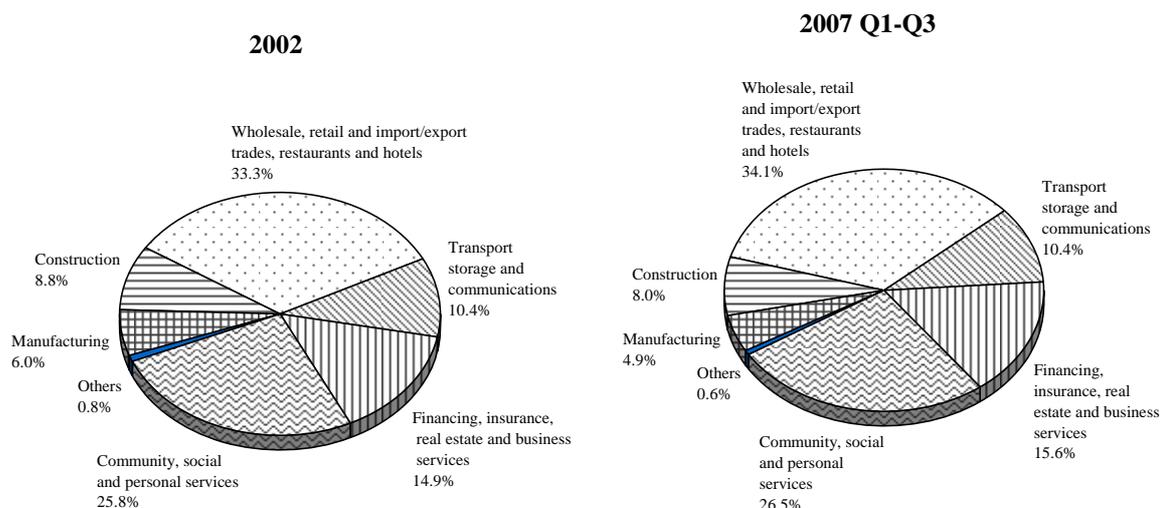
Germany -0.8

Netherland -1.2

Source: (*) Innovation at Work: The European Human Capital Index, Lisbon Council Policy Brief (2006)

This article has explained the education upgrading and experience accumulation as the key factors in driving labour productivity growth in Hong Kong. In view of the present sustained economic upturn, this increase in production capacity arising from the productivity growth will be one of the key factors in containing the overall inflation. To secure the future productivity growth, the Government will continue to play its part in investing in education and re-training, attracting talents from the Mainland and overseas, and maintaining the flexibility of the labour market.

Diagram 1.6 : Service sectors now taking up 87% of total employment*



Note : (*) These are the Composite Employment Estimates, as derived from the basic data of the General Household Survey and the Quarterly Survey of Employment and Vacancies on business establishments. Figures for 2002 refer to the annual average, while the figures for 2007 refer to the average for the first three quarters of the year.

Some highlights of economic policy

1.16 Economic policy that adheres to the principle of “Big Market, Small Government” has allowed the Hong Kong economy to remain nimble and adjust itself in a responsive manner to keep pace with the scorching pace of changes in the external environment. The robust economic growth over the past four years that made up one of the longest expansions in recent history, the consistent high ranking in international competitiveness and economic freedom surveys and the rising number of regional headquarters in Hong Kong are all evidence of success from this pro-market tradition.

1.17 Hong Kong needs to strive for development that is sustainable, balanced and diversified. Deepening the integration with the burgeoning Mainland economy will continue to be a key factor for Hong Kong to achieve sustainable development going forward. There has been significant progress on this front over the past year. In particular, a new supplement to the Closer Economic Partnership Arrangement (CEPA) was signed in June 2007, introducing 40 new liberalisation measures in 28 services areas, including 17 existing CEPA services areas and 11 new services areas. As a result, the total number of services areas covered by CEPA expanded from 27 to 38. The latest CEPA package offered a positive response to a number of recommendations in the Final Report of the Economic Summit on China's 11th Five-Year Plan and the Development of Hong Kong.

1.18 There has been notable development in fostering even closer ties between Hong Kong and Shenzhen as well. For instance, the Hong Kong-Shenzhen Western Corridor and the Shenzhen Bay Port were opened for public use in July 2007. A co-operation agreement on "Shenzhen/Hong Kong Innovation Circle" was also signed in May 2007, and co-operation between airports in Hong Kong and Shenzhen and joint development of the Lok Ma Chau Loop are being studied.

1.19 In order to expand the economy's production capacity to provide room for sustainable growth, the Government will put efforts into pushing forward infrastructure projects that could potentially result in sizeable benefits to the society and the Chief Executive highlighted ten major infrastructure projects in his Policy Address delivered in October 2007. These projects will consolidate Hong Kong's status as a global city, and the enlarged capacity and increased efficiency of the economy will also keep cost pressure down for businesses and residents in Hong Kong. Moreover, more effective cross-boundary linkages with near-by Mainland cities and provinces will help expedite the integration of Hong Kong with its hinterland.

1.20 Apart from hardware, quality of "soft infrastructure" is just as vital in putting a world-class city head-and-shoulder above its peers. Global competition for talent is as fierce as in the battle for markets, and the Government will actively pursue policies that can attract a diverse group of Mainland and overseas talent to come and contribute to the development of Hong Kong. In addition to economic strength, environmental protection and heritage conservation are also essential building blocks for a quality city and quality life for its residents. Environmental protection will require the engagement of the business sector and the public to enhance their awareness and rally their support, while heritage conservation should be emphasizing on making these legacies integral and lively parts of the local community to generate wider social and economic benefits.

1.21 Hong Kong has been widely recognised as one of the leading international financial centres, and the Government will continue to promote integration of the financial systems of Hong Kong and the Mainland through complementary development, mutual co-operation and interaction. In addition, a diversified financial market is deemed necessary in order to strengthen Hong Kong's financial centre position in light of the rapidly changing demand of investors and global financial marketplace. The issuance of renminbi-denominated bonds in 2007, efforts to attract more listing of overseas enterprises and developing an Islam finance market in Hong Kong are some of

the initiatives in this direction.

1.22 The strong economic rebound has brought about substantial improvement to household financial positions in general, but it has also contributed to rising inflation. The Government is fully aware of the impact from higher prices on local households, particularly the grassroots. With a view to build a harmonious and caring society, the Government will put forward measures in a timely manner to provide adequate and direct support to the underprivileged and ease the economic burden of the needy, making good use of the expenditure in response to the community's aspirations. Yet, the most effective and fundamental way to improve the conditions of all strata of the community is to foster overall economic development to create new employment opportunities, which will in turn raise the income of the grassroots and alleviate the impact of inflation on households.

Notes :

- (1) The Gross Domestic Product (GDP) is an overall measure of net output produced within an economy in a specified period, such as a calendar year or a quarter, before deducting the consumption of fixed capital. In accordance with the expenditure approach to its estimation, GDP is compiled as total final expenditures on goods and services (including private consumption expenditure, government consumption expenditure, gross domestic fixed capital formation, changes in inventories, and exports of goods and services), less imports of goods and services.
- (2) The seasonally adjusted quarter-to-quarter GDP series, by removing the variations that occur at about the same time and in about the same magnitude each year, provides another perspective for discerning the trend, particularly in regard to turning points. A detailed examination reveals the presence of seasonality in the overall GDP and in some of its main components, including private consumption expenditure, government consumption expenditure, exports of goods, imports of goods, exports of services, and imports of services. However, due to the presence of considerable short-term fluctuations, no clear seasonal pattern is found in gross domestic fixed capital formation. Therefore, the seasonally adjusted series of GDP is compiled separately at the overall level, rather than summing up from its main components.

CHAPTER 2 : ECONOMIC OUTLOOK FOR 2008 AND THE MEDIUM TERM

Summary

- *In 2008:*
 - *Barring any adverse economic shocks, the Hong Kong economy is forecast to expand further, at a solid pace of 4-5% in real terms. This would be slower than the rapid growth pace achieved over the past four years, but still higher than the average growth rate over the past ten years.*
 - *The external trading environment is subject to a large degree of uncertainty, as the slowdown in the US economy can be sharper than expected and as the repercussions from the global financial market turbulence have yet to fully surface. Nevertheless, the growth momentum for East Asia, particularly the Mainland economy, as well as for other major emerging markets remains fairly strong, with generally upbeat domestic demand. This together with a weaker Hong Kong dollar should render support to Hong Kong's trade performance.*
 - *Locally, both consumer and investor sentiments stay firm. The robust labour market conditions, coupled with stronger household income and wealth positions, would bolster consumption spending. The ample business opportunities arising from the economic integration with the Mainland would also induce further investment activities. The downturn in the US economy is also likely to bring about lower interest rates. Domestic demand is expected to continue to be a key driving force of overall economic growth.*
 - *Inflationary pressures are likely to persist, as food and energy prices are expected to remain elevated well into 2008. Although further labour productivity growth should provide some mitigating effect, higher wage costs and rentals on the local front and stronger price pressures from the external front along with the softness of the US dollar would continue to pose upside risks to inflation. Taking into account the various one-off factors which will push down the Composite CPI level in the year, headline consumer price inflation is forecast at 3.4%. Underlying CCPI inflation is forecast at 4.5%.*

- *The medium-term to longer-term prospects for the economy remain bright, as the strategy of leveraging on and integrating with our fast-growing economic hinterland continues to pay off. The major infrastructure projects announced in the 2007-08 Policy Address, when completed, will also increase Hong Kong's productive capacity and enhance its efficiency significantly further. The Government is also actively building up further economic links with other emerging markets, such as India and the Middle East. Coupled with the productivity uplift achieved in the process of restructuring towards a knowledge-based economy, the Hong Kong economy is expected to attain a 4.5% trend GDP growth over the next few years.*

Major external factors

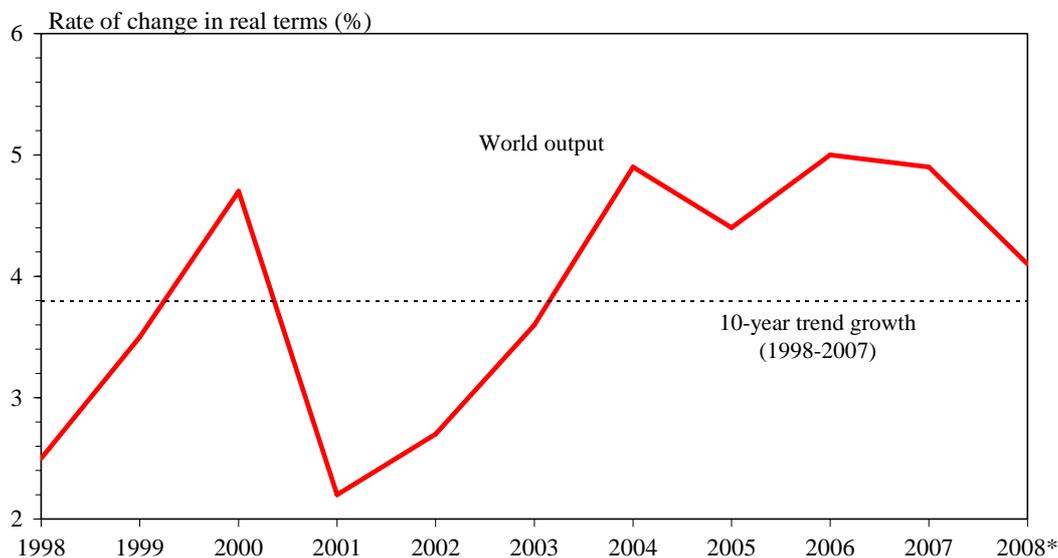
2.1 Given the small open economy nature of Hong Kong, global economic conditions are always crucial in determining the economy's fortune. The developments on the external front are, on balance, likely to be less accommodative in 2008 than in the past few years, as the near-term prospects of the advanced economies are overshadowed by the financial market turbulence and the US economic slowdown. Nevertheless, the growth momentum for East Asia, particularly the Mainland economy, and other major emerging market economies (such as India, Russia and the Middle East) has held up well, along with strong domestic demand. The latter development, together with the softness of the US dollar, should provide some support to Hong Kong's external trade. As to external price pressures, it is noted that in many parts of the world, there are persistent upside risks to inflation on account of the elevated food and energy prices on a global scale and a relatively low interest rate environment.

Global economic outlook

2.2 The global economy registered another year of buoyant performance in 2007, in spite of the waning momentum for advanced economies towards the end of the year. US economic growth in particular was dragged by its housing market downturn and subprime problems. There were signs of the housing problems spilling over into other segments of the US economy as evidenced by the rise in unemployment and slower consumption growth in the last quarter of 2007 as well as weaker service sector activities in early 2008. In Europe, economic expansion continued at a solid pace in 2007, yet the global financial turbulence had weakened both consumer and investor sentiments in the latter part of the year. In Japan, the economic recovery continued at a moderate pace, with exports providing the major impetus to growth. In contrast, the

performance of the emerging market economies was spectacular in 2007. The Mainland economy was robust and so were India, Russia and many other emerging economies in East Asia and the Middle East. According to the IMF, the contribution of the Mainland economy to global economic growth in real terms surpassed that of the US or EU in 2007. According to the World Bank, all developing economies taken together accounted for half the growth of world import demand in 2007, indicative of the upbeat domestic demand in these economies. For 2007 as a whole, the IMF estimated that the global economy attained robust growth at 4.9%, slightly cooling from the 5.0% expansion in 2006.

Diagram 2.1 : IMF forecasts the global economic growth to moderate from the buoyant pace in the past few years



Note : (*) IMF's forecast, based on purchasing power parity weights.

2.3 For 2008, the global economic prospects have been dimmed by the headwinds from the financial markets that began last summer as well as the widely expected slowdown of the US economy. In the US, the protracted housing market downturn, coupled with the tightening credit as a result of the subprime problems, is likely to weaken consumer spending and hence import demand further in the coming quarters. US economic growth is expected to be subdued during most of 2008. Likewise, the EU economies are also likely to be dragged by the adverse consequences of the continued discord in their credit markets. In some EU markets, such as the UK and Spain, there was also fallout in their housing markets. Economic growth in the EU is likely to decelerate in 2008. In Japan, economic growth is also likely to be moderate at best, as consumer confidence is still rather weak and as construction activity is likely to remain subdued due to the tightened building regulations. Meanwhile, it is

worth noting that the lingering inflationary pressures in many of these high-income economies could complicate the situation as the room available for their central banks to ease the monetary stance further would be limited.

2.4 In contrast, growth momentum in many emerging market economies, particularly the Mainland economy and other Asian economies, is expected to hold up well in 2008. Their domestic demand in general has remained strong and should provide support to a further growth in world trade. Moreover, these economies are mostly on a much sounder footing than before to withstand a slowdown in the advanced economies. However, given the sheer size of the US economy, it is difficult for the Asian region to declare a complete decoupling from the weaker US economic performance. Thus the growth pace of Asian exports is likely to slow somewhat in 2008.

2.5 Specifically on the Mainland economy, which is Hong Kong's economic hinterland and accounts for about half of Hong Kong's merchandise exports, it is widely expected to attain another year of strong growth on account of its export competitiveness and robust domestic demand. Nevertheless, the US market still directly takes up about one-fifth of the Mainland's exports. Should the US economy experience a sharper-than-expected downturn, there could be a more notable impact on the Mainland's exports. In 2008, the Mainland authorities will adopt a tight monetary policy, with a view to preventing overheating and keeping inflation under control. Although this is not likely to slow the Mainland's economic growth in a significant way, there are still uncertainties about how these cooling measures would affect the Hong Kong economy. On the other hand, the Mainland's continued efforts to promote consumption and to encourage businesses and residents to invest overseas would continue to provide a lot of business opportunities for the Hong Kong economy.

Table 2.1 : Growth forecasts for major economies in 2008⁽¹⁾

	2008		
	2007* (%)	IMF* (%)	Private sector forecast[^] (%)
World	4.9	4.1	-
Advanced economies	2.6	1.8	-
US	2.2	1.5	1.6
Euro area	2.6	1.6	1.6
Japan	1.9	1.5	1.4
Emerging market and developing economies	7.8	6.9	-
Developing Asia	9.6	8.6	-
Mainland China	11.4	10.0	10.3
India	8.9	8.4	7.9 [#]
Middle East	6.0	5.9	-

Notes : (*) World Economic Outlook Update, IMF, January 2008.
(^) Average forecast as in February 2008.
(#) Growth rate for April to March fiscal year.
(-) Not available.

Exchange rates and price competitiveness

2.6 Apart from the economic conditions in the major export markets, exchange rate movements also have implications for Hong Kong's external demand. The persistent softness of the US dollar, especially in the second half after the outburst of subprime mortgage problem and subsequently the interest rate cuts in the US, has led to a decline in the Real Effective Exchange Rate Index of the Hong Kong dollar, which in December 2007 was 6% lower than a year earlier. The lagged effects of the weakening Hong Kong dollar along with the US dollar in the latter part of 2007 should continue to help Hong Kong's export competitiveness in the early part of 2008. While currency movements could be difficult to forecast particularly in view of the on-going financial market turbulence, the prevailing market views tend to see further downside to the US dollar given the aggressive rate cuts by the Federal Reserve, the lingering housing market problem and the sizeable external imbalances of the US economy. As such, the exchange rate movements during 2008 would likely to remain conducive to Hong Kong's exports of goods and services.

2.7 The movements of renminbi exchange rates are another important aspect of Hong Kong's price competitiveness. Since the introduction of the managed float regime in July 2005, the renminbi had appreciated against the US dollar in an orderly and gradual manner. By December 2007, the renminbi had strengthened by around 13% against the US dollar since the regime change. However, most currencies also staged gains against the US dollar during the same period, with a number of currencies like the euro, Australian dollar and some Asian currencies had actually risen in value against the renminbi since they appreciated by a larger extent vis-à-vis the US dollar. Combined with the strong competitiveness of the Mainland products arising from their improving quality, the Mainland's exports growth had been basically little affected by the renminbi's appreciation against the US dollar and continued to be supportive to Hong Kong's trade growth.

2.8 While a further gradual appreciation of renminbi against the US dollar is widely anticipated for 2008, the further weakening of the US dollar vis-à-vis other currencies should offer some offsetting effect. Unless the renminbi appreciation is much larger than expected, the impact of a moderately stronger renminbi on external trade for the Mainland and Hong Kong should not be very significant. In addition, the rise in purchasing power for Mainland residents and businesses should be positive for the Hong Kong economy, in form of, among others, boosting effects to inbound tourism and demand for business services and for goods re-exported through Hong Kong.

Diagram 2.2 : US dollar sliding further

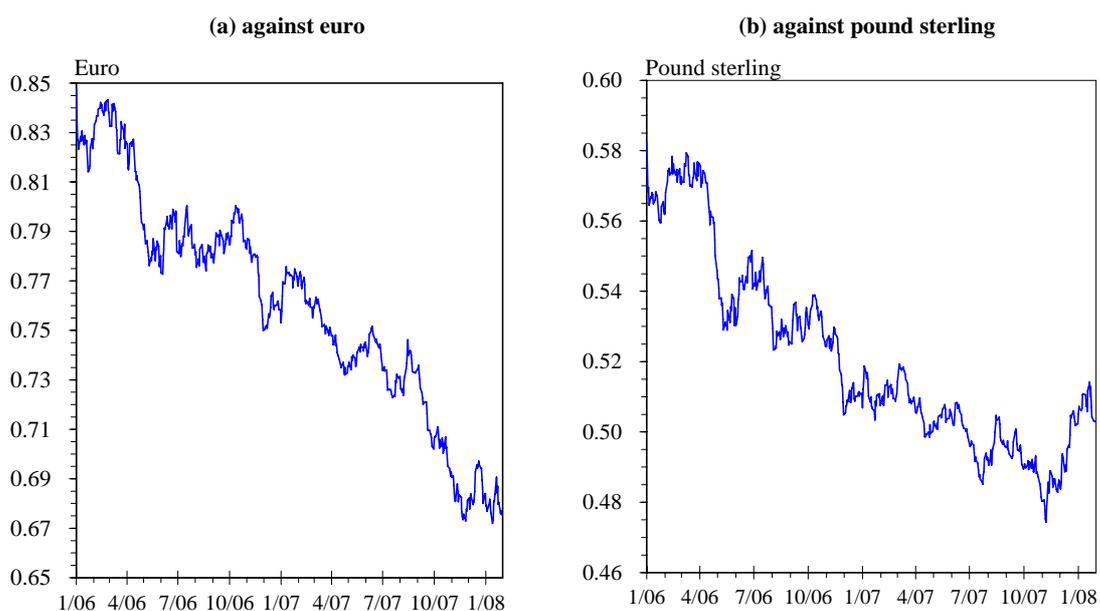


Diagram 2.2 (cont'd) :

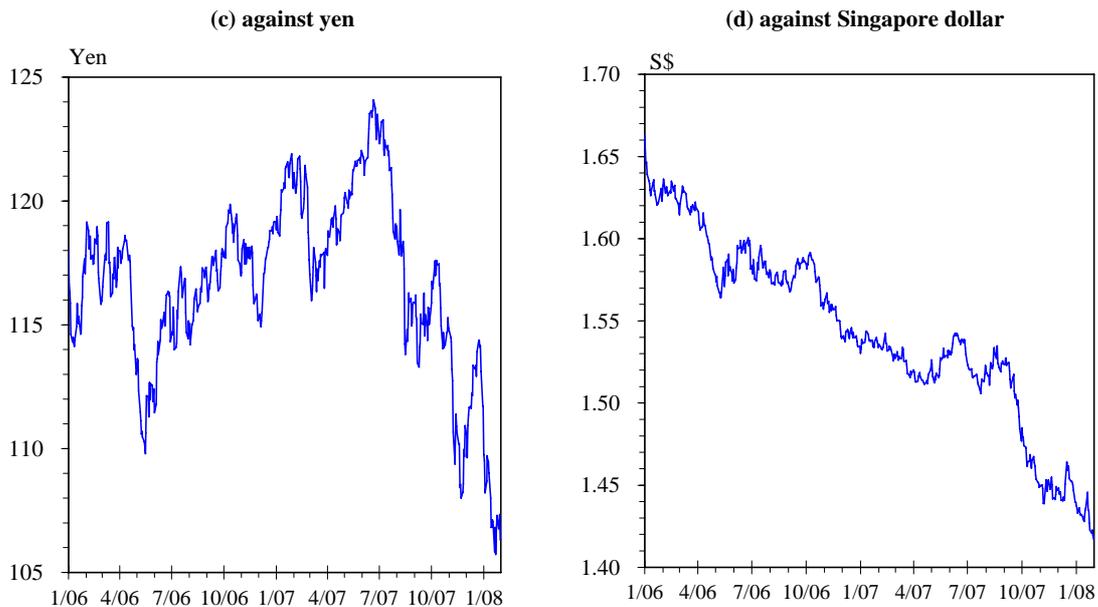
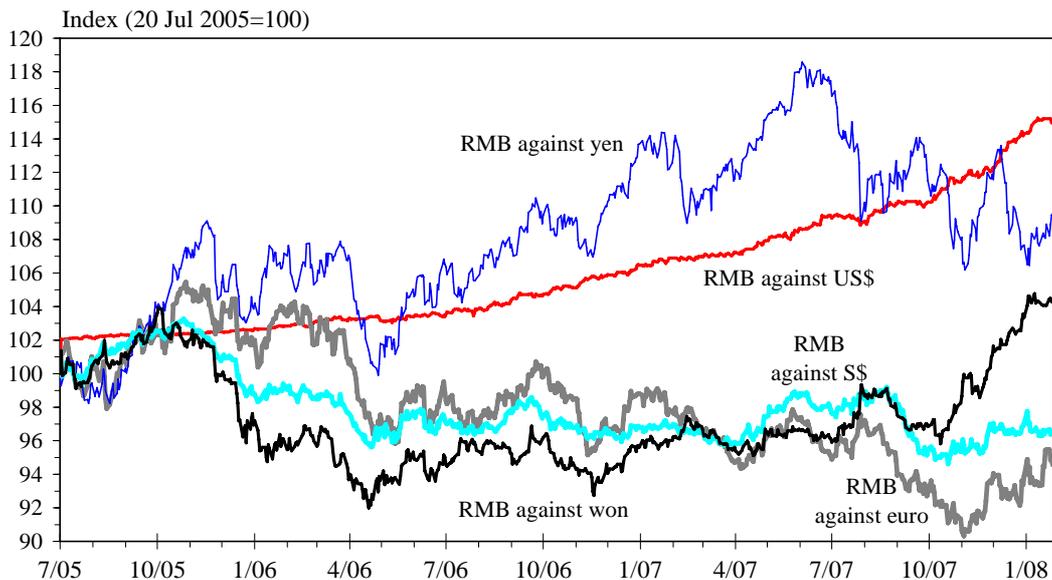


Diagram 2.3 : Movements of renminbi against other currencies are also important to Hong Kong's trade performance



Note : An increase in the index represents an appreciation of renminbi against the currency concerned.

2.9 Nevertheless, the expected further appreciation of the renminbi and weakening US dollar would continue to put upward pressure on local inflation from the external front. In 2007, import prices in overall terms rose by 2.3% over 2006, which was smaller than the corresponding fall of 4.4% in the Nominal Effective Exchange Rate Index of the Hong Kong dollar. This suggests that over the past year competition at the import level has helped to diffuse some of the inflationary pressures arising from a weaker Hong Kong dollar. However, should the appreciation of renminbi and the decline in US

dollar turn out to be faster than expected, the ramifications as far as imported inflation is concerned may become more notable.

Financial markets

2.10 The global credit market turmoil since last August has caused heightened volatilities in the financial markets. The situation is still evolving and the repercussions on the global economy will depend on whether there are further significant financial losses caused to the major financial institutions and whether the concerted efforts by the various major central banks are effective in calming the financial markets and restoring the functions of the credit markets. The turmoil has so far affected more the US and some EU economies. There are indications that the tightening credit in the advanced economies has already affected consumer spending and corporate investment in these economies and hence their economic growth. Nevertheless, the emerging market economies, including those in Asia, have been less affected. As the credit market turbulence is likely to linger on well into 2008 until the process of re-assessing and re-pricing risks is completed by the financial market participants, this year will likely see further wide fluctuations in financial markets around the world.

2.11 As an international financial centre, with strong linkages with other major financial markets in the world, the financial markets in Hong Kong will adjust in tandem with incoming news about the developments in the global economy. Given the sound institutions and strong regulatory framework in Hong Kong, our financial markets will be able to function effectively and orderly notwithstanding the wide fluctuations expected for 2008. Yet, the swiftness of capital flowing in and out of different markets and the increased connectivity among them nowadays could have potentially destabilising effect. For instance, an abrupt reversal of the ample liquidity conditions in Hong Kong could result in a sharp elimination of discount for Hong Kong dollar interbank interest rates compared with their euro-dollar deposit counterparts and hence a less accommodative monetary environment in the local economy. These are areas that need to be closely watched.

World inflation, interest rates and commodity prices

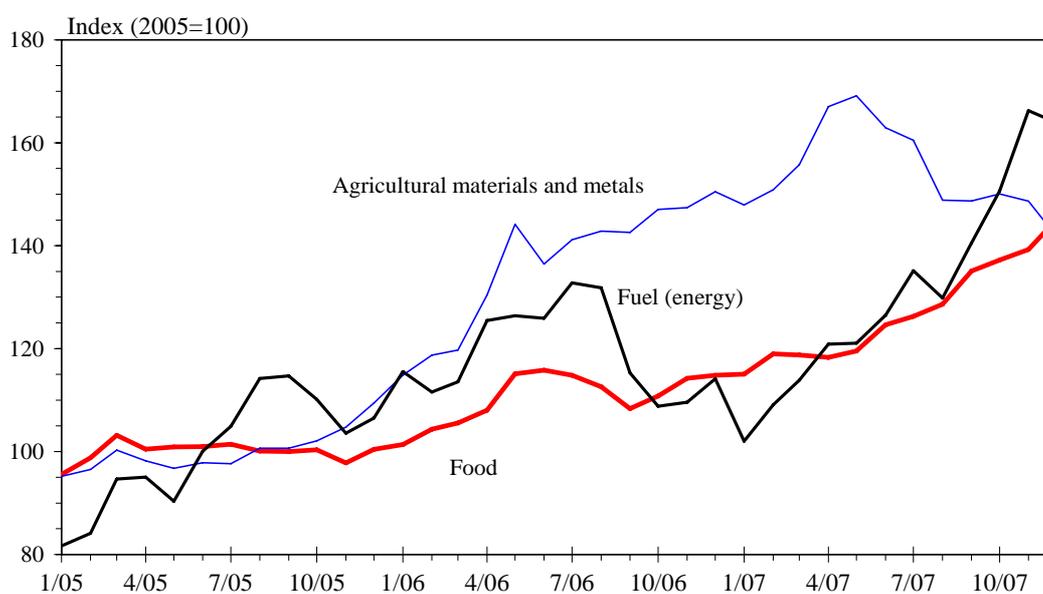
2.12 Inflationary pressures in many parts of the world have been building up over the past year, due to several years of robust global economic growth and higher food and energy prices (*Box 2.1*). Although the Federal Reserve and other major central banks are expected to lower interest rates further in the event of the global economic conditions turning worse than expected, the lingering

inflationary pressures may limit the extent of interest rate cuts that the central banks can pursue.

2.13 On commodity prices, of particular note in 2007 were the run-up of oil prices in the latter part of the year and the sustained surge in food prices worldwide. High oil prices and hence fuel costs tend to cut into the purchasing power of consumers in the advanced economies. The problem of thin spare capacity in oil supply is exacerbated by occasional supply disruptions and unstable regional geopolitical environment in major oil-producers. Thus oil prices are likely to remain elevated in the near term. Since Hong Kong is not an oil-dependent economy, the impact of high oil prices has so far been rather modest. Yet the upward pressures on transport and electricity costs have been increasing.

2.14 As to food prices, the increase over the past year was substantial. According to the IMF's world food price index, the increase showed no sign of abating, accelerating to 22% year-on-year in the fourth quarter of 2007. Given the strong demand for food-crops arising from the production of bio-fuels and the time lag required for food supply to catch up with demand, world food prices are likely to stay high well into 2008. On the other hand, prices of other commodities for industrial uses, including agricultural materials and metals, tended to ease or stabilise in the latter part of last year, in anticipation of slower demand growth arising from the weaker economic performance of the advanced economies.

Diagram 2.4 : Global food and energy inflation likely to remain elevated well into 2008



Note : Indices as depicted refer to IMF's commodity price indices.

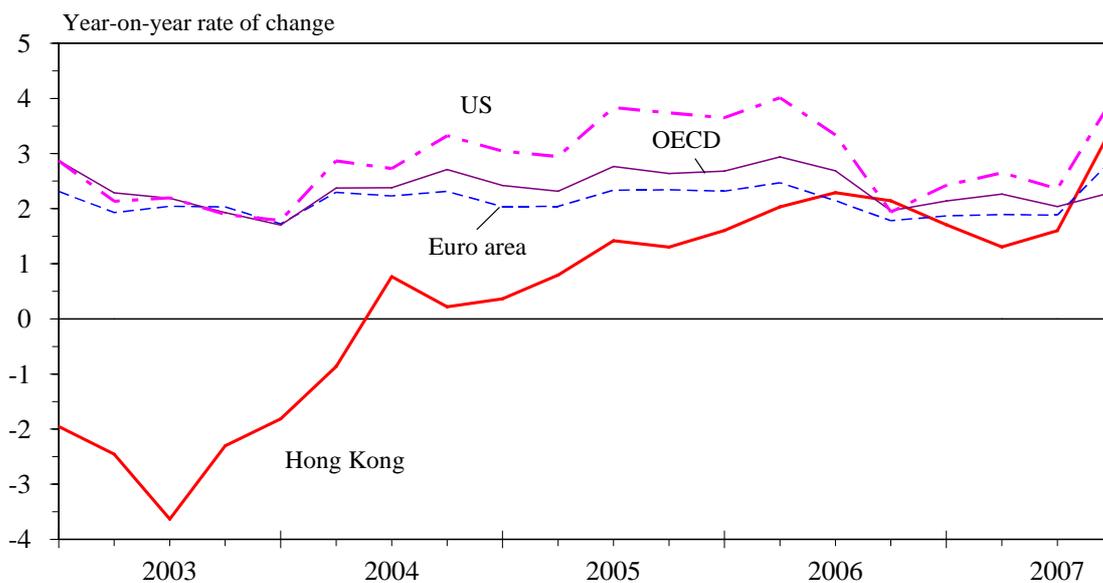
Box 2.1

Hong Kong's inflation in global context

Average inflation in the advanced economies has been low since the early 1990s, largely on account of the efforts by these economies in adopting more independent monetary policy and prudent fiscal stances. The advanced economies learned the hard lessons from the experience in the 1970s, when inflation shot up to double-digit levels. Productivity growth, especially through the IT revolution, as well as competition brought about by globalisation and the rise of the low-cost emerging market economies have also been contributory to the recent low inflation era. Although the declines in inflation in the major emerging market economies have lagged behind those in advanced economies, world inflation on the whole has been rather moderate over the past decade or so. According to the IMF, world inflation averaged at 4.0% over the past decade. In the US and euro area, the corresponding figures were 2.6% and 2.0%.

However, inflationary pressures have been building up in many parts of the world more recently. This is particularly evident in the major emerging market economies, including the mainland of China, India and Russia. Inflation in the advanced economies, though still contained, has also picked up to levels outside their comfort zones.

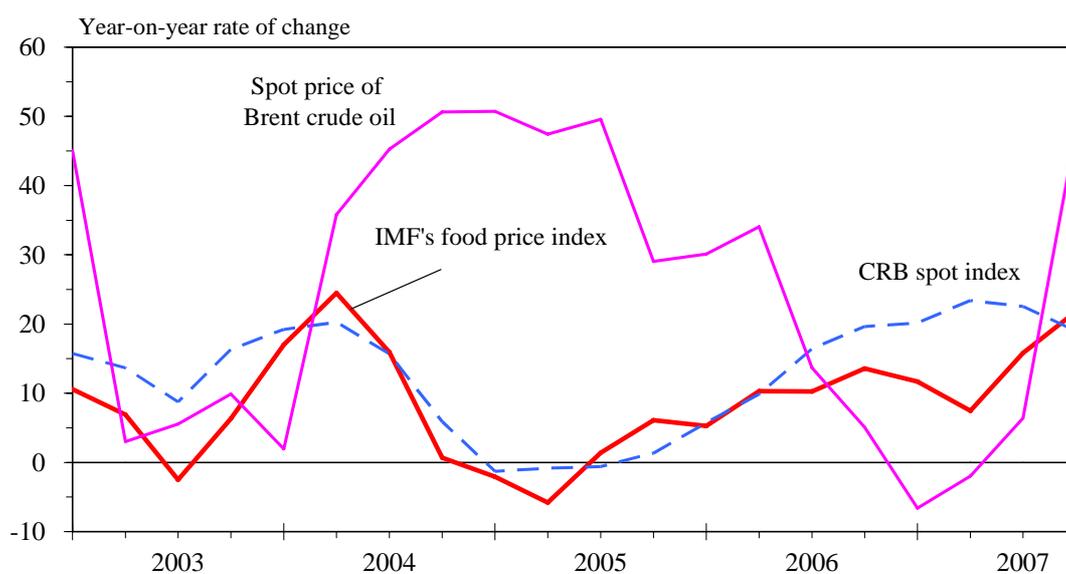
Inflation in advanced economies



Box 2.1 (Cont'd)

Several major developments have tended to push up world inflation. Firstly, global economic expansion over the past several years has been the strongest in decades. A number of advanced economies began to run against their capacity constraints in 2007, as evidenced by the continuous falls in their unemployment. Secondly, there has been strong demand for food, oil and other commodities, as a result of the robust global economic conditions. The fast-growing emerging market economies, while contributing to the softness of prices of manufacturing products over the past decade, are often cited as a major source of new demand leading to the surges in food and other commodity prices. Also, the increased use of food crops for production of biofuels has contributed in a significant way to global food inflation. Thirdly, the near-term economic outlook for the advanced economies and indeed the global economy is dimmed by the credit market turmoil triggered by the US subprime problems as well as the downturn of the US economy. As a result, the advanced economies have to adopt a looser monetary policy stance to forestall economic downturn, thus allowing some inflationary pressures to build up.

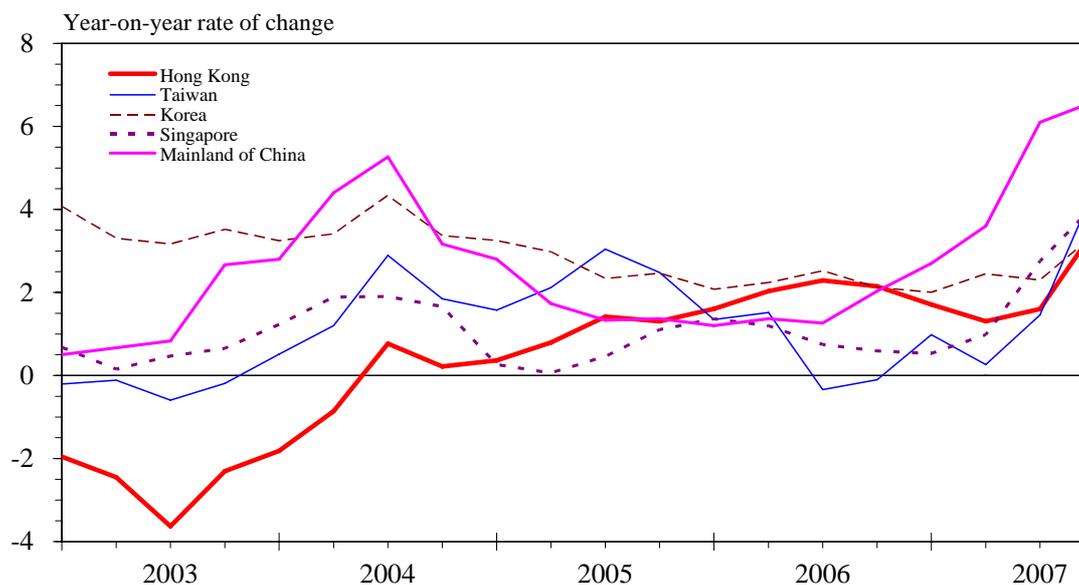
Food, oil and other commodity prices



In Hong Kong, inflation has become a concern. Yet the CPI inflation rate in Hong Kong in the fourth quarter of 2007, at 3.5%, was actually comparable to the situation in the relatively advanced economies. Specifically, our inflation rate was similar to or lower than the corresponding rates in the US (4.0%) and other Asian economies at a similar stage of economic development, like Singapore (4.1%), Taiwan (4.5%) and Korea (3.4%). Thus it is worth noting that the inflationary pressures facing Hong Kong are by and large part of a more worldwide phenomenon.

Box 2.1 (Cont'd)

Inflation in Asia



The return of the unpleasantly high inflation rates on a global scale as experienced in the 1970s is highly unlikely, as fighting inflation is still the chief objective of the governments of the major economies over the medium term. Indeed, inflation expectations in the advanced economies at this juncture are still well-anchored. Having said this, elevated inflationary pressures may still persist in the coming years. It is also worth noting that price adjustments in Hong Kong in response to changes in the global economic environment are part and parcel of Hong Kong's flexible market mechanism, which helps to balance the demand and supply of various goods and services. Although Hong Kong's inflation rate is not high when compared with many other places in the world, the Government is still very concerned about the impact of inflation on the lower-income families and the elderly and will continue to assist these people to weather the hardship.

Major downside risks

2.15 The global economy, though likely to expand moderately further in 2008, is subject to a range of downside risks. *Firstly*, the US economic situation may turn out to be worse than expected. The subprime market turmoil, if lingers on, may lead to further notable contraction of the US housing market, which in turn may worsen the mortgage markets and other credit markets, resulting in a vicious circle. The impacts on the global economy could be more long lasting and severe than currently anticipated. *Secondly*, the repercussions of the financial market turbulence have yet to fully play out. If the financial losses to investors and financial institutions are much larger than expected, markets for an even wider range of financial products may be affected. *Thirdly*, the US current account deficit remains alarmingly large, although the

weakening of the US dollar over the past years has helped narrow such a deficit somewhat. A disorderly adjustment of the external imbalances, if happened, would cause more disruptions in the global economy, including exchange rate fluctuations and abrupt unwinding of yen carry-trade. *Fourthly*, protectionist sentiments are warming up in the US and the EU. This will increase the uncertainty surrounding our trading environment.

Outlook for the Hong Kong economy in 2008

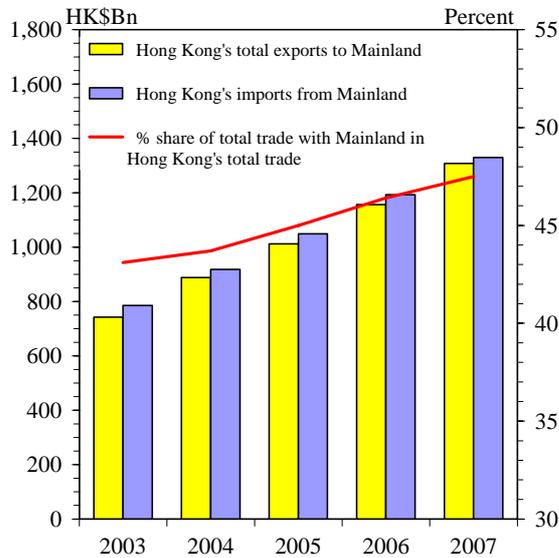
2.16 Barring any adverse economic shocks, the Hong Kong economy is likely to attain another year of solid expansion. The growth pace should, however, be slower than the rapid growth rates achieved over the past four years, in view of the weaker external environment arising from the softness of the US economy and the financial market turbulence. Hong Kong's close links with the still fast-growing Mainland economy, as well as other Asian economies which have sustained fairly strong growth momentum, should continue to provide opportunities for Hong Kong businesses to display their resilience and dynamism in 2008.

2.17 Externally, the trade outlook turns much more uncertain this year, as the growth prospects for the advanced economies are overshadowed by the weak US economy and possible repercussions of the financial market turmoil. The EU and Japan economies are likely to expand further, providing some support on the trade front. More importantly, the growth momentum for East Asia, particularly the Mainland economy, and similarly for other major emerging market economies like India and Russia, is expected to remain fairly robust in 2008, thereby helping offset the weakness of the advanced economies. A further decline of the US dollar, if occurs, will also render some support to Hong Kong's external competitiveness. Overall, unless the US economic slowdown is much sharper than expected, *total exports of goods* are likely to grow further in 2008, albeit at a pace probably slower than in 2007.

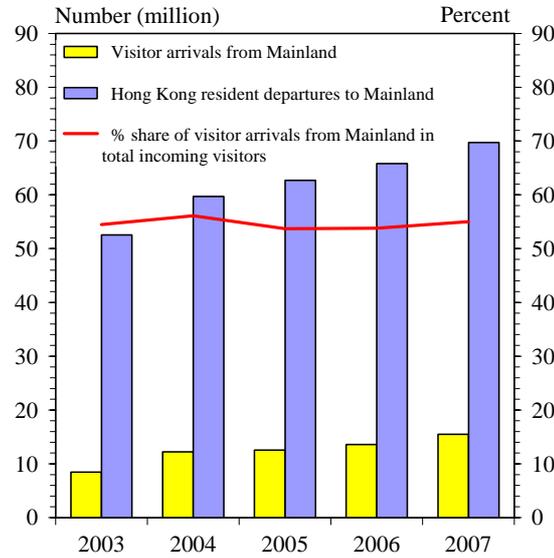
2.18 The outlook for *exports of services* is more positive. Inbound tourism has been strong, boosted by the rising incomes of Mainland residents and the appreciation of the renminbi. The weakness of the US dollar has also induced more overseas visitors to Hong Kong. Hong Kong's offshore trade will also continue to benefit from the Mainland's strong trade flows. The on-going integration with the Mainland on economic and financial fronts should continue to render support to exports of finance, business and other services, although the growth pace may be slower than the rapid increases in previous years.

Diagram 2.5 : The strategy of integrating with the Mainland continues to payoff

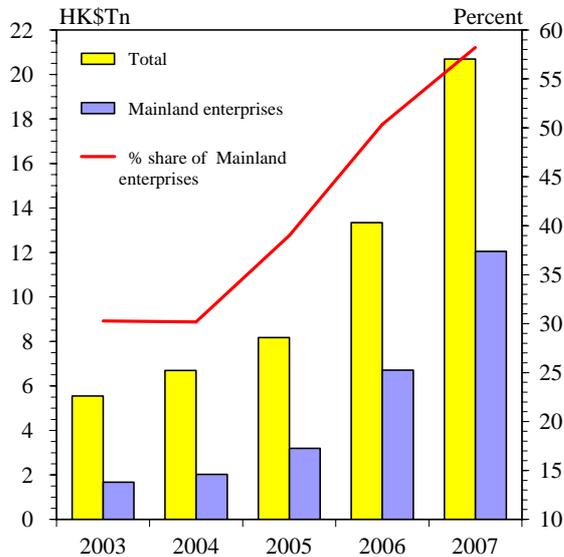
(a) Merchandise trade



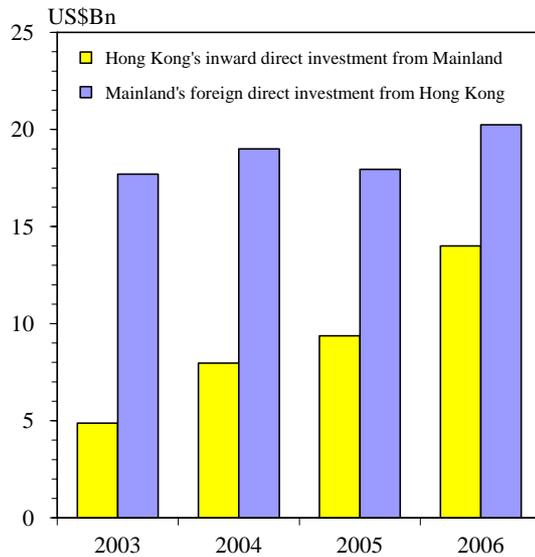
(b) Visitor arrivals from Mainland and Hong Kong resident departures to Mainland



(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



2.19 Locally, both consumer and investor confidence should hold up firmly. The strong economic upturn over the past four years, as well as the rises in household income and wealth, have strengthened the willingness of consumers to spend. Yet the uncertainty in the performance of the asset markets in 2008 is an area to watch out. The abundant business opportunities arising from the economic and financial integration with the Mainland should also induce further investment activities in 2008. Indeed, the results of the latest Business Tendency Survey conducted by the Census and Statistics Department

confirm that large companies surveyed remained optimistic about the near-term business outlook. The lower interest rate environment, though largely a reflection of the weak US economic conditions, will also help support both consumption and investment demand. Thus in 2008 *domestic demand* is expected to remain a key driving force for overall economic growth at a time when external demand is subject to a greater degree of uncertainty.

Diagram 2.6 : Consumer confidence likely to stay strong

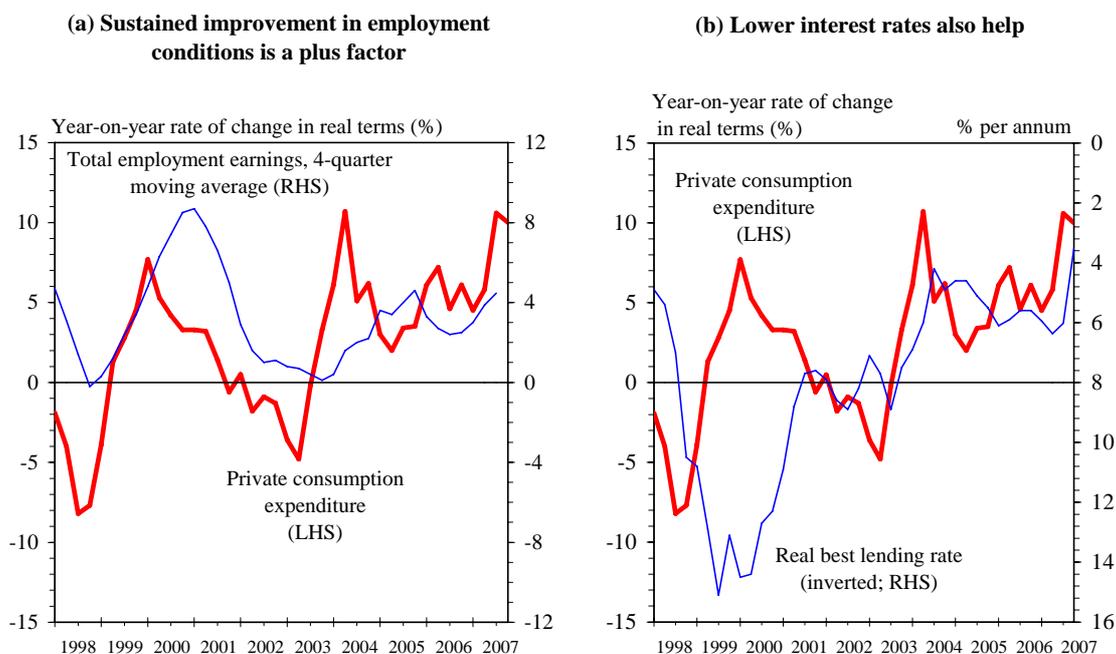


Diagram 2.7 : Consumer sentiment will also depend on asset market performance

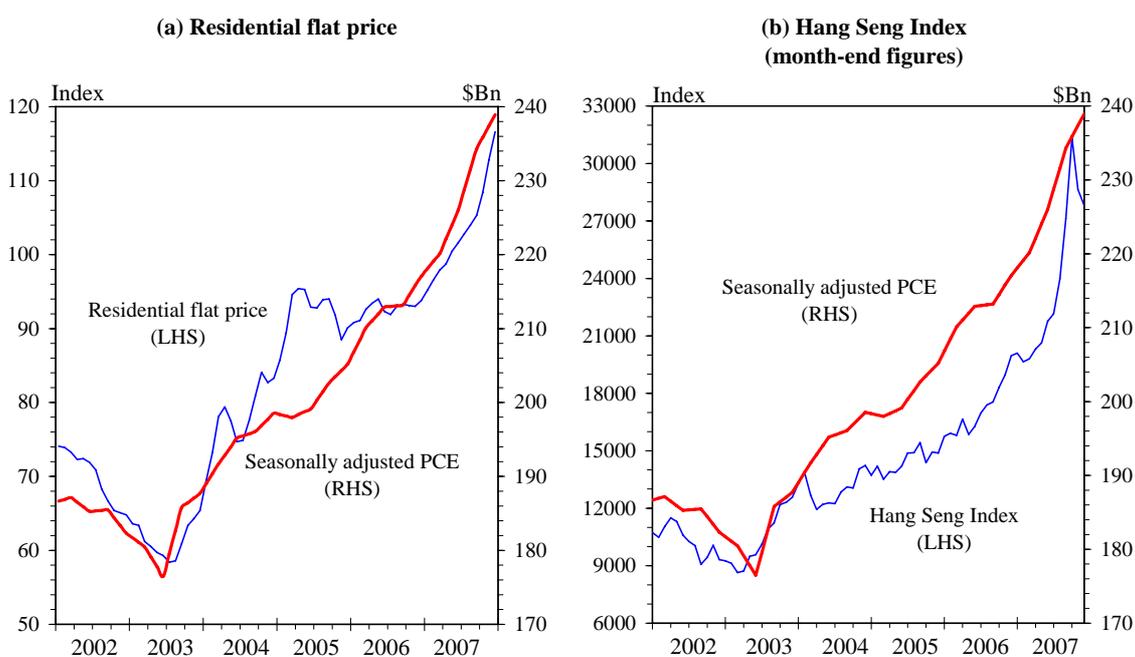
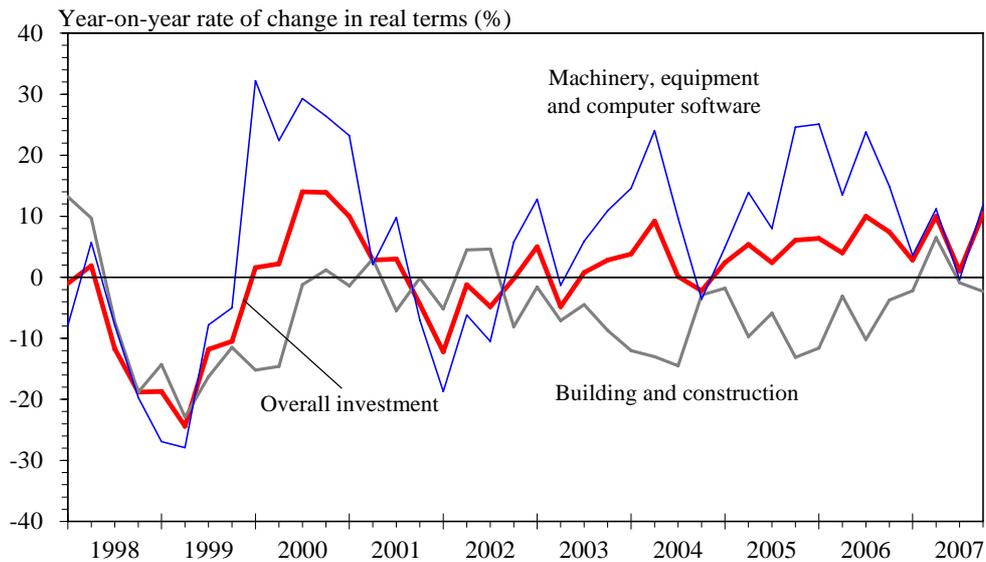
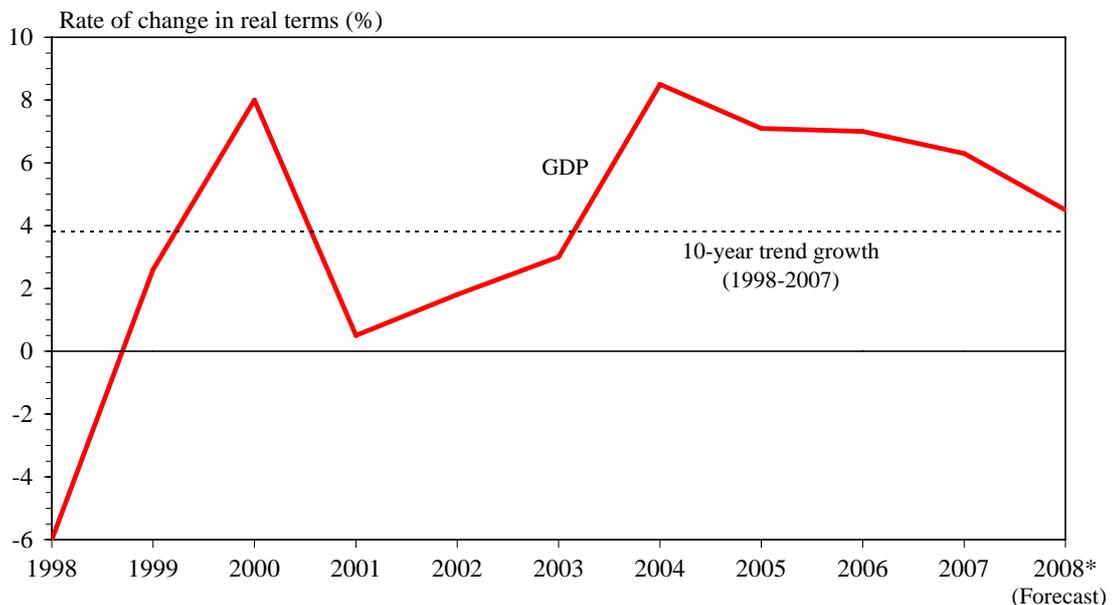


Diagram 2.8 : Integration with the Mainland should induce further investment activities



2.20 Overall, barring any abrupt adverse developments on the external front, the Hong Kong economy is expected to expand further, at 4-5% in real terms in 2008. Although this would be less rapid than the robust growth pace achieved over the past four years, the forecast growth rate, if realised, would still be higher than the average growth rate of 3.8% over the past ten years. This range forecast is also largely in line with the prevailing forecasts by the private sector, which generally suggest a further solid expansion of the Hong Kong economy at a pace mostly in the range of 4.5–5.5%.

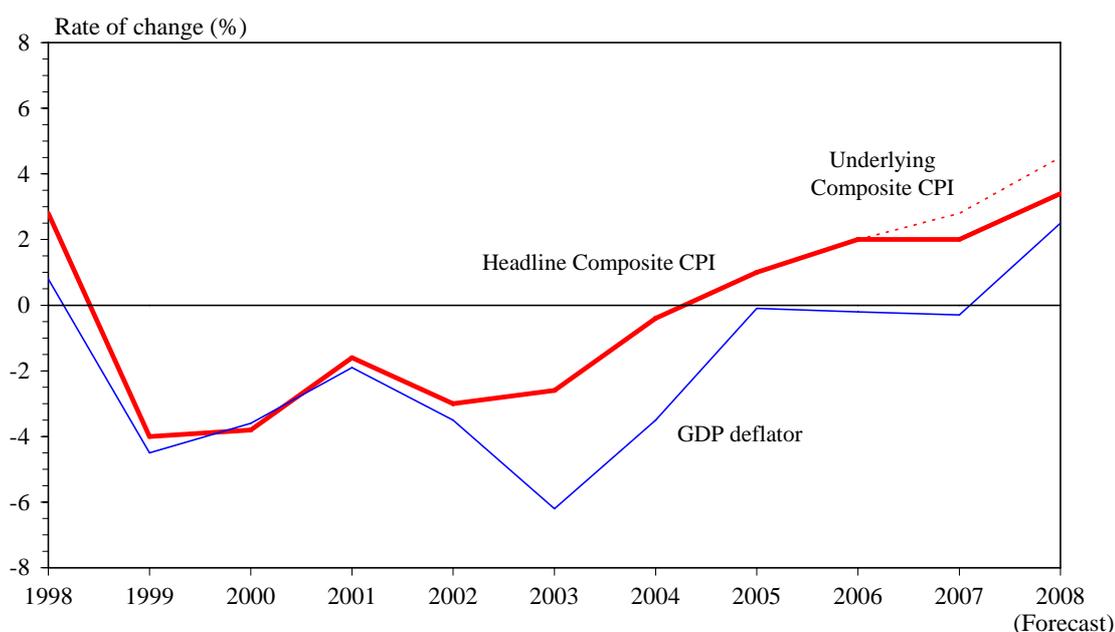
Diagram 2.9 : Barring any adverse economic shocks, the economy should grow solidly further in 2008



Note : (*) Mid-point of the range forecast.

2.21 Consumer price inflation has been climbing up over the course of 2007 alongside the sustained robust expansion of the economy and the surge in food prices. Looking forward, the underlying inflationary pressures are likely to remain elevated in 2008. Global food inflation shows no sign of abating. Given the lag time required for world food supply to catch up with demand, higher food prices are likely to persist well into 2008. Meanwhile, the run-up of oil prices in the latter part of last year will exert upward pressures on transport fares and utility charges. Also, the gradual appreciation of the renminbi and the likely further weakening of the US dollar may result in higher import prices. As the economy is expected to continue to expand solidly further and consumption demand to stay rather strong, there may be a larger degree of pass-through from import prices to retail prices. Locally, private housing rentals have been rising and this will eventually reflect in the housing cost component of the Consumer Price Indices. The tightened labour market would also exert stronger upward pressures on wage costs. Yet the related one-off Budget measures announced for 2008/09 would lower the Composite CPI level. For 2008 as a whole, the headline *Composite CPI* is forecast to increase by 3.4%. Netting out the effects of the one-off factors, the underlying Composite CPI is forecast to increase by 4.5%. The *GDP deflator* is forecast to rise by 2.5%, largely reflecting the increase in domestic prices and the expected fall in terms of trade due to a weaker US dollar.

Diagram 2.10 : Inflation will go up further in 2008



Forecast rate of change in 2008 (%)

Gross Domestic Product (GDP)

<i>Real GDP</i>	4-5
<i>Nominal GDP</i>	6.5-7.5
<i>Per capita GDP, in real terms</i>	3.1-4.1
<i>Per capita GDP at current market prices</i>	HK\$245,900-248,200 (US\$31,500-31,800)

Composite Consumer Price Index

<i>Headline</i>	3.4
<i>Underlying</i>	4.5

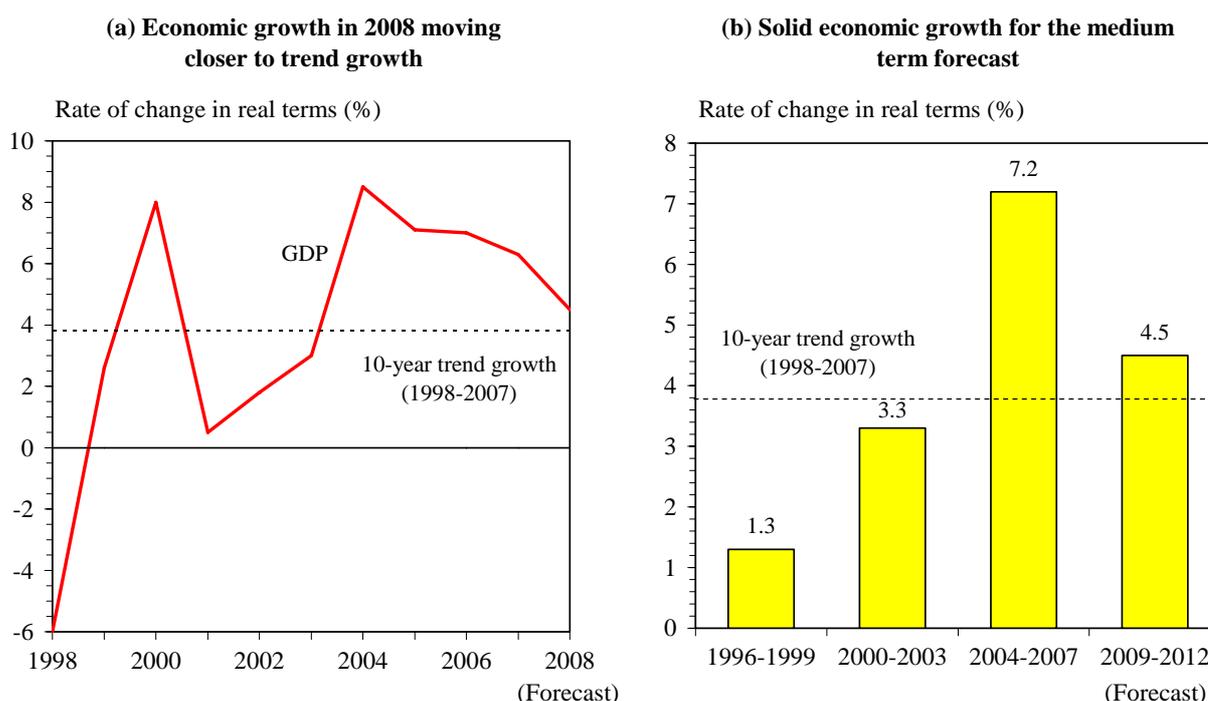
GDP Deflator	2.5
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Medium-term outlook for the Hong Kong economy

2.22 The medium-term prospects for the economy remain bright, as the strategy of leveraging on and integrating with our fast-growing economic hinterland continues to pay off. The action agenda from the Economic Summit on the National 11th Five-Year Plan will help Hong Kong to establish its vital role in the economic development of our country. By end-2007, over 110 specific measures recommended by the Action Agenda have been implemented. These will also further deepen and broaden our economic and financial links with the Mainland under the CEPA framework and Pan-PRD cooperation, thereby bringing significant benefits to both sides. The Government is also building up further our links with other emerging markets, such as India and the Middle East. On the supply side, the Hong Kong economy will continue to shift towards higher value-added services and knowledge-based activities in the coming years. The quality of Hong Kong's workforce has been improving in terms of educational attainments and skills. Hong Kong will further enhance its status as an international financial centre and a regional hub for trade, logistics, tourism and business. The productivity growth achieved in the process will help the economy attain a 4.5% trend GDP growth over the next four years 2009-2012. The Government will also push ahead the major infrastructure projects, which will create jobs and bring benefits to the economy during the construction phase. When completed, these facilities will enhance the production capacity and efficiency of the Hong Kong economy and further our integration with the Mainland, thereby bringing significant benefits to the community over the longer run.

2.23 With sustained economic expansion, higher labour and housing costs, as well as price pressures from the external front, inflation will continue to be an issue that deserves close attention over the medium term. Indeed, higher inflationary pressures now appear to be a global phenomenon. Over the medium term, underlying composite CPI inflation is likely to remain at around 4% per annum. Apart from the issues of global inflation and the health of the US economy, several other challenges prevailing in the external environment will likely linger on over the medium term. The global trade imbalances, though tending to stabilise over the past year, are still alarmingly large. A disorderly and abrupt adjustment will entail unwelcome disruptions in the global economy. A related issue is the persistent protectionist sentiment from the US and EU against Mainland products, increasing the risk to Hong Kong's trade. The risks associated with the heightened volatility in financial and exchange rate markets may persist and cannot be ignored. Domestically, the structural shift of Hong Kong economy to knowledge-based activities, in response to the forces of globalisation, regional competition and the rapid transformation of the Mainland economy, may lead to greater challenges for the lower-skilled workers. Also, the ageing population will have profound implications on our health care and social welfare systems, as well as on the public finance, over the medium and longer run. In view of all these challenges, it is important for the Government to maintain flexible markets and exercise prudence in its fiscal policy.

Diagram 2.11 : Medium-term economic outlook remains bright



Note :

- (1) The economic forecasts for major economies cited in this report are mainly for the purpose of illustration and are not purported to be exhaustive. Economic forecasts from a variety of sources, including the World Bank, the central banks and government departments in the respective economies and certain private sector forecasting agencies, have been taken into account in deriving the forecasts for Hong Kong's exports.

CHAPTER 3 : THE EXTERNAL SECTOR

Summary

- *Merchandise exports grew notably further in 2007, although the growth pace moderated somewhat in the second half of the year. The robustness of the Mainland market and the strength of most EU and Asian markets more than offset the impact arising from the lacklustre performance of the US and Japanese markets. The enhanced external price competitiveness brought about by the weakness in the US dollar also helped.*
- *With total exports to the Mainland market continuing to grow sturdily on the back of its strong domestic demand and trade flows, the share of the Mainland market in Hong Kong's total exports increased further to 49% in 2007. Also, the sustained growth momentum of the Asian region also lent support to intra-regional trade during the year. This helped mitigate the dampening effects arising from a slowing US economy and the heightened uncertainty brought about by the global financial market turbulence.*
- *Exports of services were robust throughout 2007, showing double-digit growth over the course of the year. Exports of trade-related services continued to grow sharply upon the vibrant trade flows in the Mainland. The financial market boom during the year led to continued surge in exports of financial services. Exports of travel services also grew markedly, benefiting from the strong performance of inbound tourism.*
- *During 2007, various policy measures were implemented to strengthen Hong Kong's external competitiveness. The Closer Economic Partnership Arrangement (CEPA) and its four supplements will enhance mutual economic co-operation between Hong Kong and the Mainland, and provide impetus for the growth of Hong Kong's service industries. With the implementation of the Supplement IV to CEPA in January 2008, the number of service areas enjoying the liberalised measures has increased to 38. The 2007-08 Policy Address announced ten major infrastructure projects for promoting economic development, among which the four cross-boundary infrastructure projects will enhance the flow of people and goods between the Mainland and Hong Kong. This will strengthen further the role of Hong Kong as an international business, trading and logistics centre.*

Visible trade

Total exports of goods

3.1 Merchandise exports sustained another year of notable growth in 2007. *Total exports of goods* (comprising re-exports and domestic exports) grew by 8.3% in real terms⁽¹⁾ in 2007, after a strong increase of 10.2% in 2006. The global economy remained robust during most part of 2007, but the weakness of the US economy turned more evident in the latter part of the year, being dragged by its protracted housing market downturn and sub-prime mortgage problems, and the financial market turmoil also weakened consumer confidence in the advanced economies. Reflecting this, the growth of total exports slowed modestly to 7.2% year-on-year in the second half of 2007, from an average of 9.6% in the first half. The Mainland's vibrant trade flows remained the key driving force for Hong Kong's exports. The general weakness of the US dollar, sustained steady expansion of the European Union (EU) and strong performance of many other Asian markets also rendered support to the export growth.

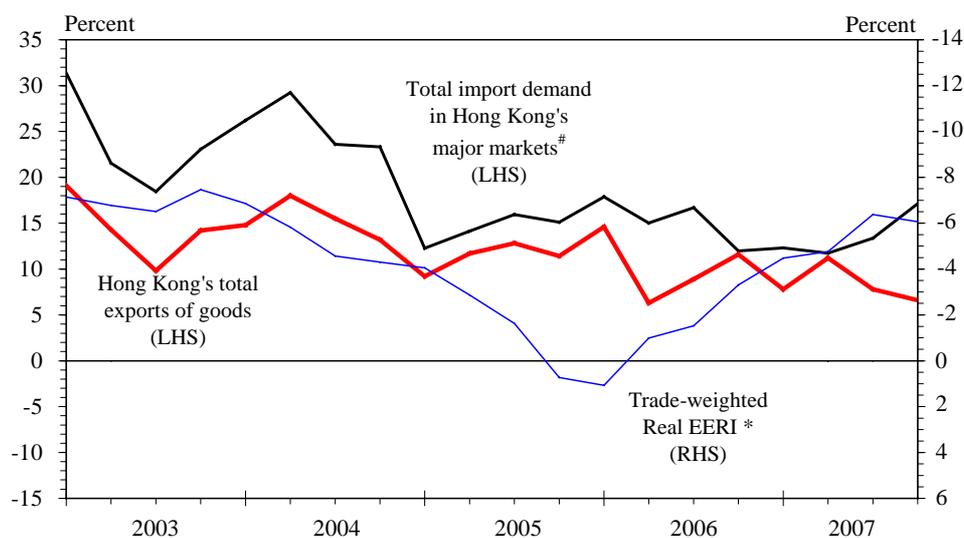
**Table 3.1 : Total exports of goods, re-exports and domestic exports
(year-on-year rate of change (%))**

	<u>Total exports of goods</u>			<u>Re-exports</u>			<u>Domestic exports</u>					
	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>			
2006 Annual	9.4	10.2	1.0	10.0	10.8	1.1	-1.1	1.1	-2.1			
Q1	12.1	14.6	(3.3)	-0.3	10.7	13.2	(3.7)	-0.2	38.7	42.3	(-0.9)	-2.9
Q2	5.4	6.3	(0.0)	0.6	4.6	5.3	(0.8)	0.9	19.9	23.9	(-10.6)	-3.9
Q3	8.4	8.9	(4.4)	1.4	9.4	9.8	(5.1)	1.5	-6.1	-4.2	(-7.2)	-1.3
Q4	11.9	11.6	(2.9)	1.9	15.3	14.9	(4.2)	2.0	-31.8	-30.9	(-18.9)	-0.8
2007 Annual	9.2	8.3	2.3	10.8	9.9	2.4	-18.9	-19.8				0.8
Q1	9.0	7.8	(0.8)	2.7	11.8	10.6	(0.9)	2.8	-33.4	-33.5	(-0.6)	0.4
Q2	11.7	11.2	(2.7)	2.0	13.5	13.1	(2.4)	2.1	-18.4	-19.4	(8.2)	0.6
Q3	8.2	7.8	(0.9)	2.0	10.0	9.6	(1.3)	2.1	-20.9	-21.0	(-7.9)	0.8
Q4	8.2	6.6	(1.8)	2.7	8.6	7.1	(1.9)	2.8	-0.7	-3.4	(0.0)	1.0

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

3.2 *Re-exports*⁽²⁾ continued to be the key growth driver and outperformed overall export growth, leaped by 9.9% in real terms in 2007, after a 10.8% increase in 2006. Strong growth momentum was maintained, though with some ease-back in the latter part of the year. *Re-exports* continued to benefit from the Mainland's strong trade flows as well as the robust intra-regional trade. The share of re-exports in total exports increased further to 95.9% in 2007, from 94.5% in 2006. In contrast, *domestic exports* fell distinctly by 19.8% in real terms in 2007, reverted from a modest increase of 1.1% in 2006.

**Diagram 3.1 : Merchandise exports continued to show notable growth in 2007
(year-on-year rate of change)**



Notes : Total exports of goods as depicted refer to the year-on-year rate of change in real terms, while total import demand in Hong Kong's major markets as depicted refers to the year-on-year rate of change in US dollar terms in the aggregate import demand in East Asia, the United States and the European Union taken together.

(*) The real EERI in this graph is inverted in scale for easier comprehension. A positive change denotes real appreciation of the Hong Kong dollar.

(#) Import demand figure for the fourth quarter of 2007 is based on information available up to November 2007.

Diagram 3.2 : Re-exports remained the key growth driver of total exports

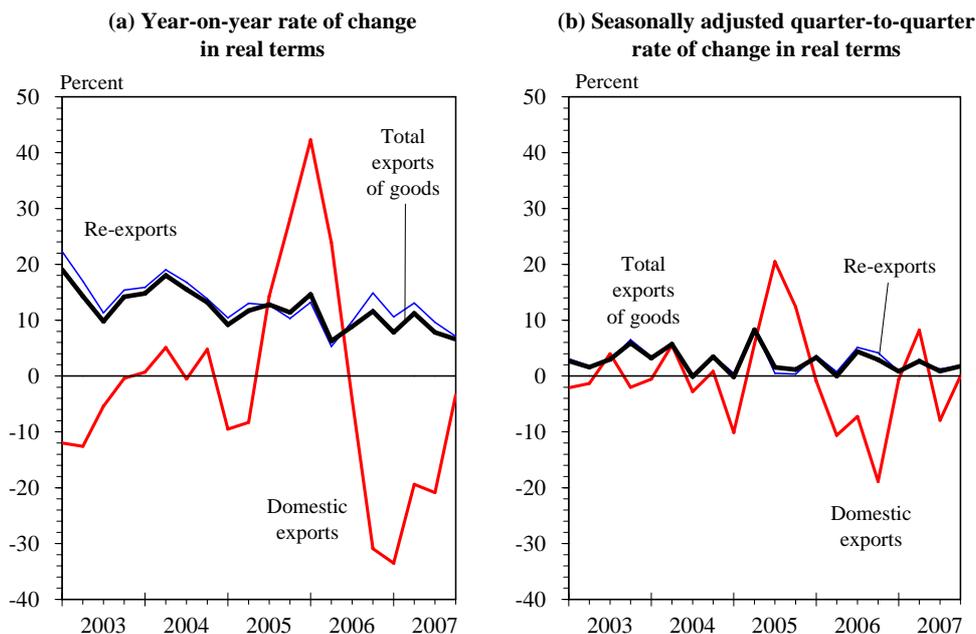
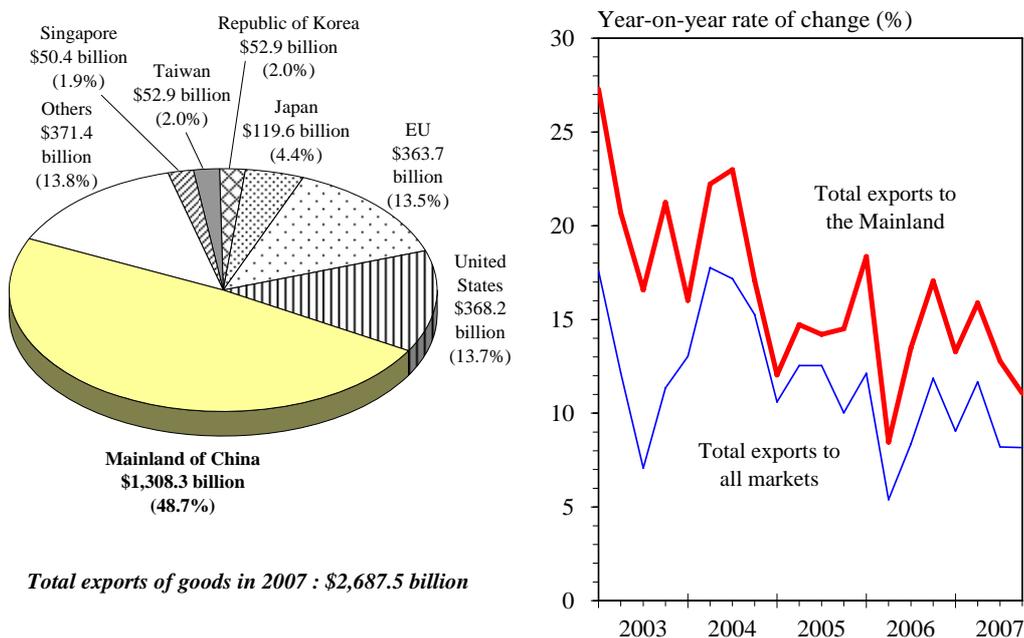


Diagram 3.3 : The Mainland market is the main engine of export growth



**Table 3.2 : Total exports of goods by major market
(year-on-year rate of change in real terms (%))**

		<u>Mainland of China</u>	<u>United States</u>	<u>European Union</u>	<u>Japan</u>	<u>Republic of Korea</u>	<u>Taiwan</u>	<u>Singapore</u>
2006	Annual	16.7	1.7	4.7	2.4	8.8	4.3	4.5
	Q1	23.1	3.5	9.5	8.2	20.9	10.4	2.3
	Q2	11.4	-2.4	4.1	3.0	12.0	-5.3	-5.4
	Q3	15.8	-1.1	1.9	0.6	10.7	8.3	12.8
	Q4	17.5	7.0	4.1	-1.4	-5.4	4.2	8.3
2007	Annual	12.9	-2.5	3.8	-0.8	0.0	-0.2	1.0
	Q1	13.1	0.7	2.7	0.6	-8.9	-1.4	0.7
	Q2	15.5	1.0	5.2	4.0	3.8	9.0	3.9
	Q3	12.9	-3.9	4.3	-5.9	0.2	-3.2	0.2
	Q4	10.7	-6.6	3.2	-1.6	5.2	-4.1	-0.2

3.3 Analysed by market, the strong uptrend of total exports to the Mainland continued and posted double-digit growth for six consecutive years, amidst its strong trade flows and robust domestic demand. Exports to such Asian emerging markets as India, Malaysia, Thailand, Vietnam and Indonesia also saw notable expansion. By comparison, exports to the other major East Asian economies, including Taiwan, Korea and Singapore, were rather lacklustre. Exports to the EU held up firm, especially those to Germany, Netherlands and France, in tandem with the steady expansion of the EU economy. The appreciation of euro should have also rendered some support to exports to the EU.

3.4 On the other hand, exports to the US reverted to a decline in 2007 with the set back concentrated in the second half of the year. This was conceivably due to the softness of the market in the wake of the housing market downfall and the turmoil arising from the sub-prime mortgage problem. Likewise, exports to Japan exhibited mild contraction in 2007 due to its weakness in import demand.

Diagram 3.4 : Exports to the Mainland remained strong

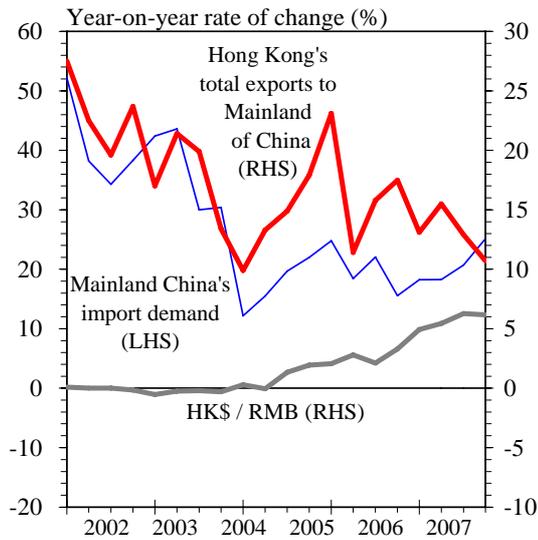
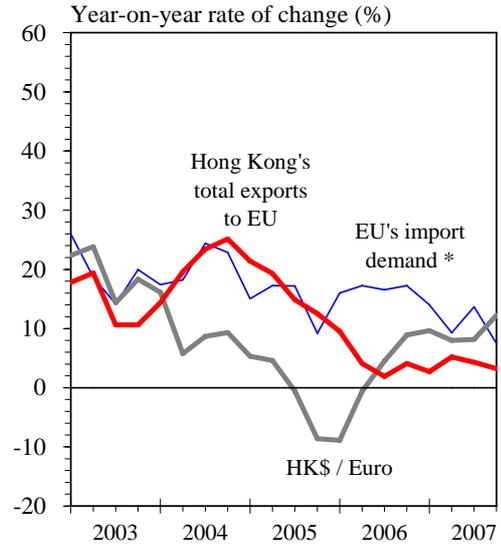


Diagram 3.5 : Exports to EU was helped by steady economic expansion in EU and the euro appreciation



Note: (*) Import demand figure for the fourth quarter of 2007 is based on information available up to November 2007.

Diagram 3.6 : Exports to US slacked further in tandem with its weakening import demand

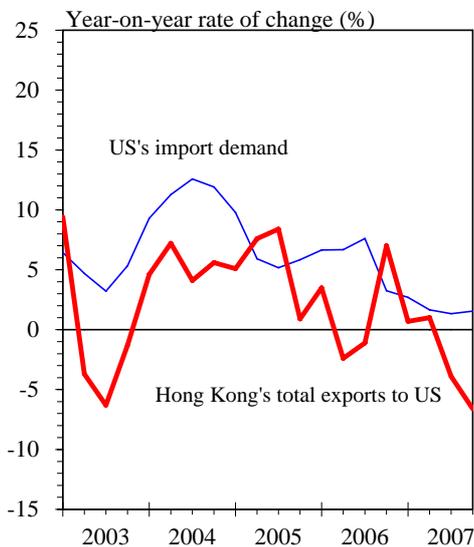
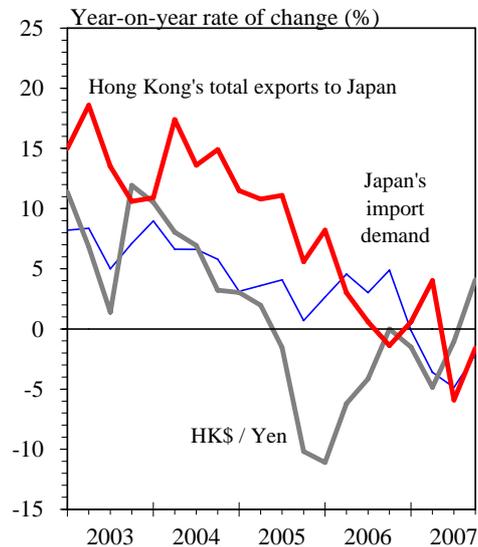
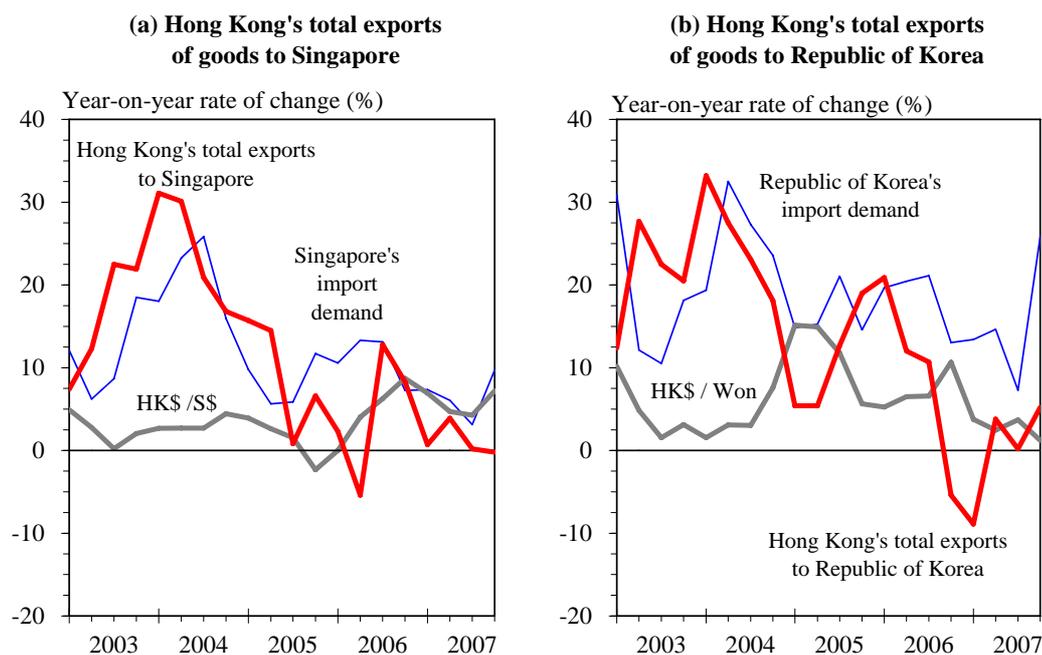


Diagram 3.7 : Exports to Japan reverted to a decline amidst the weak domestic demand



**Diagram 3.8 : Exports to Singapore and Korea moderated,
mainly due to a fall-off on raw materials intake**



Imports of goods

3.5 *Imports of goods* recorded a pronounced growth of 10.4% in real terms in 2007, after a strong increase of 10.2% in 2006. While the surge in intake for subsequent re-exporting continued, *retained imports*, referring to the imports for domestic uses, rose visibly by 11.7% in real terms in 2007, reflecting the prevailing strength of domestic demand on the back of strong consumer and investor confidence. Within this, growth in retained imports of consumer goods and foodstuffs accelerated over the course of 2007, largely tallied with the strong performance of retail sales. Likewise, retained imports of raw materials and semi-manufactures surged during most of the year. Moreover, retained imports of capital goods, which usually exhibit a certain degree of volatility, rose notably further despite the high base of comparison in the previous year.

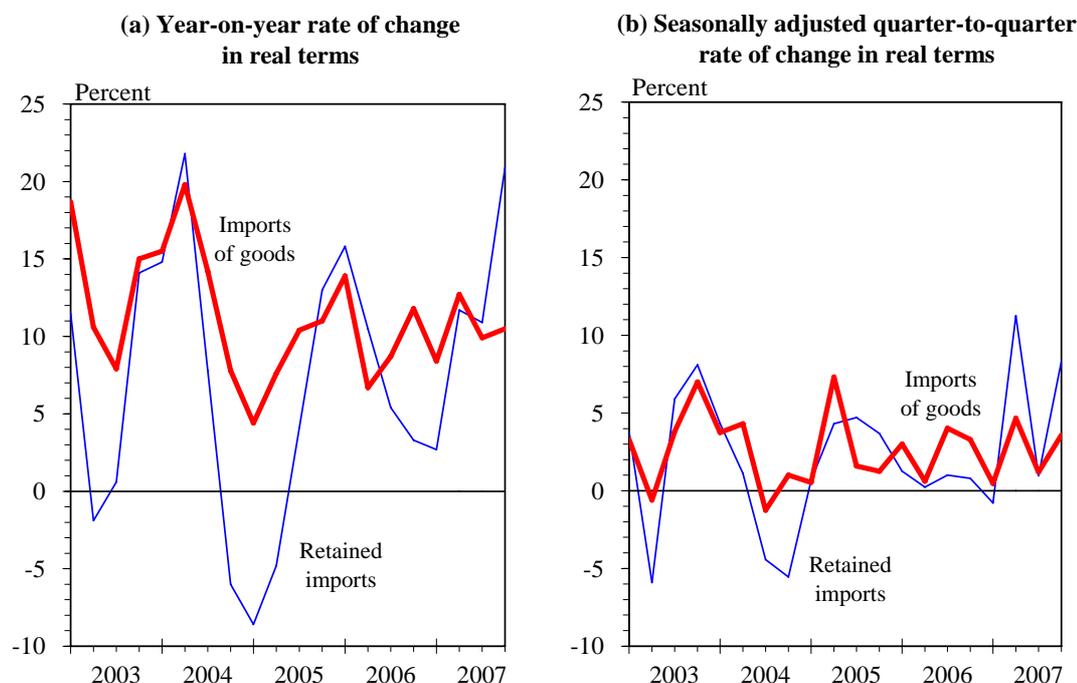
**Table 3.3 : Imports of goods and retained imports
(year-on-year rate of change (%))**

		<u>Imports of goods</u>			<u>Retained imports</u> ^(a)		
		<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>
2006	Annual	11.6	10.2	2.1	14.3	8.4	3.2
	Q1	13.8	13.9	(3.0)	20.8	15.8	(1.3)
	Q2	8.1	6.7	(0.6)	16.7	10.5	(0.2)
	Q3	10.7	8.7	(4.0)	12.7	5.4	(1.0)
	Q4	14.0	11.8	(3.3)	8.2	3.3	(0.8)
2007	Annual	10.3	10.4	2.3	8.8	11.7	1.9
	Q1	9.0	8.4	(0.5)	1.5	2.7	(-0.8)
	Q2	12.6	12.7	(4.7)	10.3	11.7	(11.3)
	Q3	9.1	9.9	(1.2)	6.6	10.9	(1.0)
	Q4	10.5	10.5	(3.6)	16.3	20.9	(8.3)

Notes : (a) Based on the results of the Annual Survey of Re-export Trade conducted by the Census and Statistics Department, re-export margins by individual end-use category are estimated and adopted for deriving the value of imports retained for use in Hong Kong.

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

Diagram 3.9 : Total imports grew briskly



**Table 3.4 : Retained imports by end-use category
(year-on-year rate of change in real terms (%))**

		<u>Consumer goods</u>	<u>Foodstuffs</u>	<u>Capital goods</u>	<u>Raw materials and semi-manufactures</u>	<u>Fuels</u>
2006	Annual	14.4	2.0	27.6	-16.8	5.4
	Q1	16.9	4.3	38.4	-6.4	4.0
	Q2	37.3	4.8	19.8	-13.4	-4.9
	Q3	7.8	2.3	32.5	-27.5	3.5
	Q4	0.5	-2.9	22.2	-18.9	19.5
2007	Annual	6.4	6.6	11.1	18.5	8.5
	Q1	-1.0	4.4	6.4	-2.9	8.6
	Q2	2.3	3.5	14.2	16.1	24.4
	Q3	6.6	8.9	1.6	33.7	-0.8
	Q4	17.7	9.7	22.0	29.3	4.7

Invisible trade

Exports of services

3.6 *Exports of services* grew distinctly further, by 11.2% in real terms in 2007, following an already strong growth of 10.1% in 2006. The appreciable growth was across-the-board throughout the four quarters of 2007. Exports of trade-related services, the largest component within exports of services and comprising mainly offshore trade, continued to surge under the support of strong intra-regional trade as well as the Mainland's robust trade flows. Exports of financial services showed a spectacular performance along with the buoyant financial market activities. Exports of travel services also showed rapid growth amidst the rapid expansion of inbound tourism. The weakening of the Hong Kong dollar along with the US dollar rendered further boost to visitor spending. Meanwhile, exports of transportation services, benefited from the vivid trade flows and strong influx of incoming visitors, continued to hold up well.

Diagram 3.10 : Trade-related and transportation services accounting for over 60% of service exports, reflecting the important role of Hong Kong as a trading hub

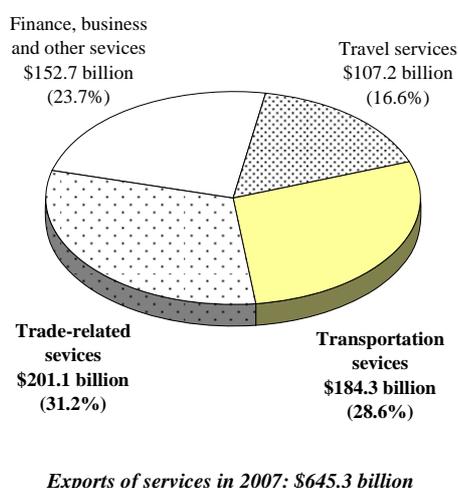


Diagram 3.11 : Notable growth in exports of services accelerated further and across the broad

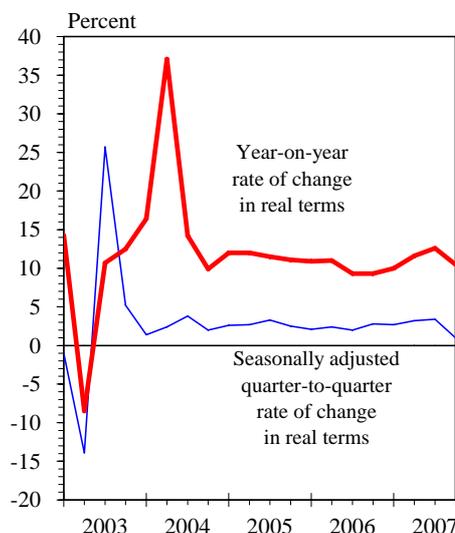


Table 3.5 : Exports of services by major service group (year-on-year rate of change in real terms (%))

Of which :

		Exports of services	Trade-related services ^(a)	Transportation services	Travel services ^(b)	Finance, business and other services
2006	Annual	10.1	8.8	8.0	6.4	18.9
	Q1	10.9 (2.1)	11.1	9.0	8.9	14.4
	Q2	11.0 (2.4)	8.6	9.7	6.0	20.3
	Q3	9.3 (2.0)	9.3	6.4	4.6	18.9
	Q4	9.3 (2.8)	6.8	6.9	6.4	22.3
2007	Annual	11.2	10.2	4.8	13.3	20.6
	Q1	10.0 (2.7)	9.6	3.9	10.9	18.7
	Q2	11.6 (3.2)	11.2	6.3	10.3	21.5
	Q3	12.6 (3.4)	11.4	5.8	14.8	23.5
	Q4	10.5 (1.0)	8.9	3.4	16.9	19.0

Notes : (a) Comprising mainly offshore trade.

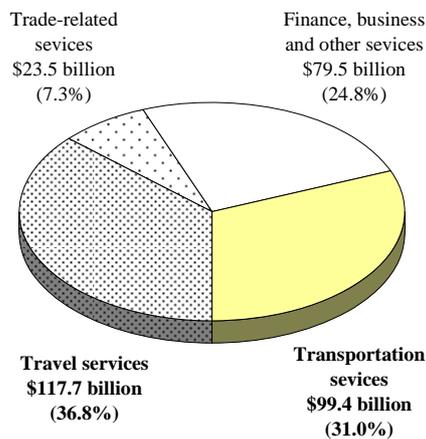
(b) Comprising mainly inbound tourism receipts.

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

Imports of services

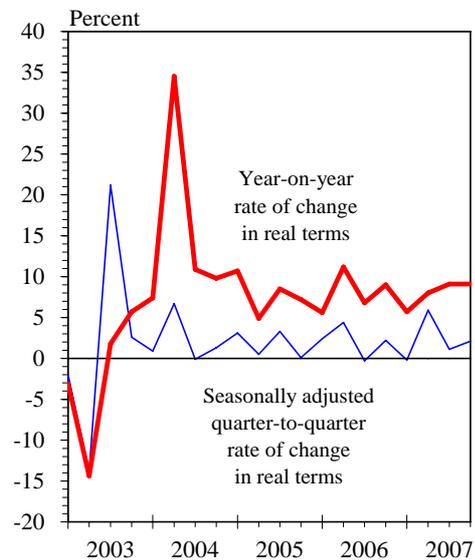
3.7 *Imports of services* rose by 8.1% in real terms in 2007, at the same pace as 2006. Imports of travel services continued on a steady uptrend, reflecting the increase in the number of residents traveling abroad. Imports of transportation services and trade-related services grew strongly on the back of the thriving trade flows. In tandem with the financial market boom and the continued robust business activities, imports of financial, business and other services recorded another year of distinct growth.

Diagram 3.12 : Travel service, transportation services, and services involving finance and business are the main components in imports of services



Imports of services in 2007: \$320.1 billion

Diagram 3.13 : Imports of services rose notably further



**Table 3.6 : Imports of services by major service group
(year-on-year rate of change in real terms (%))**

		<i>Of which :</i>					
		<u>Imports of services</u>	<u>Travel services⁽⁺⁾</u>	<u>Transportation services</u>	<u>Trade-related services</u>	<u>Finance, business and other services</u>	
2006	Annual	8.1	4.1	10.4	11.2	10.9	
	Q1	5.6	(2.4)	0.2	10.0	7.7	
	Q2	11.2	(4.4)	9.1	13.3	11.7	
	Q3	6.8	(-0.3)	1.1	9.0	12.2	
	Q4	9.0	(2.2)	6.6	9.6	11.7	
2007	Annual	8.1	4.6	6.3	10.8	15.1	
	Q1	5.7	(-0.2)	1.9	3.0	14.0	
	Q2	8.0	(5.9)	3.9	6.6	15.9	
	Q3	9.1	(1.1)	6.2	6.4	16.7	
	Q4	9.1	(2.1)	6.1	8.9	13.9	

Notes : (+) Comprising mainly outbound travel spending.

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

Visible and invisible trade balance

3.8 With the surplus in the invisible trade account more than offset the deficit in the merchandise trade account, a sizeable surplus of \$171.5 billion was recorded in the combined visible and invisible trade balance in 2007, equivalent to 5.4% of the total value of imports of goods and services. This compared with the corresponding figure of \$168.2 billion (equivalent to 5.9% of the total value of import of goods and services) in 2006. The continued sizeable surplus is a reflection of Hong Kong's strong external competitiveness in the global economy.

**Table 3.7 : Visible and invisible trade balance
(\$Bn at current market prices)**

		<u>Total exports</u>		<u>Imports</u>		<u>Trade balance</u>		
		<u>Goods</u>	<u>Services</u>	<u>Goods</u>	<u>Services</u>	<u>Goods</u>	<u>Services</u>	<u>Combined</u>
2006	Annual	2,467.4	565.1	2,576.3	287.9	-109.0	277.2	168.2
	Q1	538.5	130.3	568.3	65.8	-29.8	64.5	34.7
	Q2	586.7	130.1	622.1	69.3	-35.4	60.8	25.4
	Q3	667.2	148.9	685.8	77.0	-18.6	71.9	53.3
	Q4	674.9	155.8	700.2	75.8	-25.2	80.0	54.7
2007	Annual	2,698.9	645.3	2,852.5	320.1	-153.7	325.2	171.5
	Q1	587.3	147.6	621.5	71.1	-34.2	76.4	42.2
	Q2	656.5	148.3	702.7	76.6	-46.2	71.7	25.5
	Q3	722.1	172.0	749.4	86.5	-27.4	85.5	58.1
	Q4	733.0	177.4	778.8	85.8	-45.9	91.6	45.7

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

Trade policy and other developments

3.9 External trade will continue to play an important role in the Hong Kong economy. In this regard, the Government has made strenuous efforts to open up new business opportunities for Hong Kong's companies in respect of both trade in goods and services.

Enhancing co-operation with the Mainland under CEPA

3.10 In order to enhance opportunities for Hong Kong businesses and reinforce Hong Kong's comparative advantages in better tapping the potential of the Mainland market, the Supplement IV to CEPA was signed on 29 June 2007. It contains 40 liberalisation measures in 28 services areas, including 17 existing services areas⁽³⁾ and 11 new services areas⁽⁴⁾. The new liberalisation measures came into effect starting 1 January 2008.

3.11 As at end-2007, the Trade and Industry Department (TID) and five Government Approved Certificate Organisations issued 29 989 certificates of Hong Kong origin (CEPA) to goods produced in Hong Kong, involving a total of \$11.2 billion worth of goods. TID also issued 1 900 certificates of Hong Kong Service Supplier. The Government will continue to work closely with the Mainland authorities on further liberalisation measures under CEPA for the benefits of the Hong Kong economy.

Strengthening connectivity with the PRD

3.12 The new Shenzhen Bay Bridge was completed and has commenced operation on 1 July 2007. Along with the opening of the new border control point at the new Bridge, the HKSAR and Shenzhen governments signed a Memorandum on co-location arrangement at the Shenzhen Bay Port. The commencement of operation of the new Bridge signifies closer integration and co-operation between Hong Kong and Shenzhen.

3.13 On 10 October 2007, the Policy Address announced four cross-boundary infrastructure projects, including (1) The Guangzhou-Shenzhen-Hong Kong Express Rail Link; (2) The Hong Kong-Zhuhai-Macao Bridge; (3) Hong Kong-Shenzhen Airport Co-operation, for which the feasibility of a rail connection between Hong Kong International Airport and Shenzhen Airport will be studied; and (4) Hong Kong-Shenzhen Joint Development of the Lok Ma Chau Loop. These projects, when completed, will further facilitate the flow of people and goods between Hong Kong and the Mainland and help further strengthen Hong Kong's external competitiveness and its role as an international business, trading and logistics centre, which in turn will generate huge economic benefits to the Hong Kong economy.

Other developments

3.14 It is vital for Hong Kong to foster closer economic ties with the emerging market economies in different parts of the world, which have been assuming an increasingly important role in the global economy. According to the World Bank, emerging market economies accounted for half of the growth in world import demand in 2007. Over the past year, high-level Government delegations visited such emerging market economies as Kuwait, Saudi Arabia, the United Arab Emirates, Slovakia, Hungary, Estonia and Russia, with a view to bringing about more business opportunities for Hong Kong companies.

3.15 Against the background of a series of adjustment in processing trade policy in the Mainland, Hong Kong enterprises with manufacturing operations in the PRD have to seriously consider industrial restructuring, upgrading and relocation. The Government has been working closely with industry and taken a multi-pronged approach to help them better respond to the Mainland's measures, including relaying to the Central Government industry concerns, proposing to the Central Government other flexible measures to match with the policy adjustment, exploring with the provinces and industry alternative operating bases and helping investors obtain first-hand information about the investment

environment. The Government also plans to improve the Small and Medium Enterprises Funding Schemes and help industries to upgrade production facilities and explore new markets.

Notes :

- (1) Changes in merchandise exports and imports in real terms are derived by discounting the effect of price changes from changes in the value of the trade aggregates. Estimates of price changes for the trade aggregates are based on changes in unit values, which do not take into account changes in the composition or quality of the goods traded, except for some selected commodities for which specific price indices are available. The real growth figures reported here are based on the constant price measures adopted for compiling the external trade quantum index numbers. They are not strictly comparable with the real trade aggregates under GDP (reported in Chapter 1) which are based on the chain volume measures using the preceding-year prices as weights for aggregating the components.
- (2) Re-exports are those goods which have previously been imported into Hong Kong and are subsequently exported without having undergone in Hong Kong any manufacturing processes which change permanently the shape, nature, form or utility of the goods.
- (3) They are legal, medical and dental, real estate, job intermediary, convention and exhibition, telecommunications, audiovisual, distribution, insurance, banking, securities, tourism, cultural, maritime transport, air transport, road transport, and individually-owned stores.
- (4) They are computer and related services, market research, services related to management consulting, public utility, building-cleansing, photographic, printing, translation and interpretation, environmental services, social services, and sporting services.

CHAPTER 4 : DEVELOPMENTS IN SELECTED SECTORS

Summary

- *The residential property market, having consolidated for more than a year, showed a distinct pick-up in 2007 amidst rising income and an improving job market. Sentiment in the latter part of the year was particularly upbeat, boosted by successive interest rate cuts and increasing expectation of further interest rate easing down the road. The non-residential segment continued to fare well extensively on the back of the general trend of business expansion.*
- *The growth momentum in inbound tourism sustained well in 2007, with both overall visitor arrivals and total tourism expenditure soaring to new heights.*
- *The logistics sector continued to benefit from the sustained notable growth in external trade as well as vibrant growth in transshipment cargo flows. Both air and port cargo flows registered further expansion in 2007, although the growth pace stayed modest amidst intense competition in the region.*
- *The Government is pressing ahead with a number of large-scale domestic and cross-boundary transport infrastructure projects. On-going progress has been made in the preparatory works and co-operation with our neighbourhood in the Pearl River Delta.*
- *Hong Kong and the Mainland have been developing deeper and more extensive collaboration in innovation and technology, with a view to generating synergy from the respective strengths to mutual benefit.*

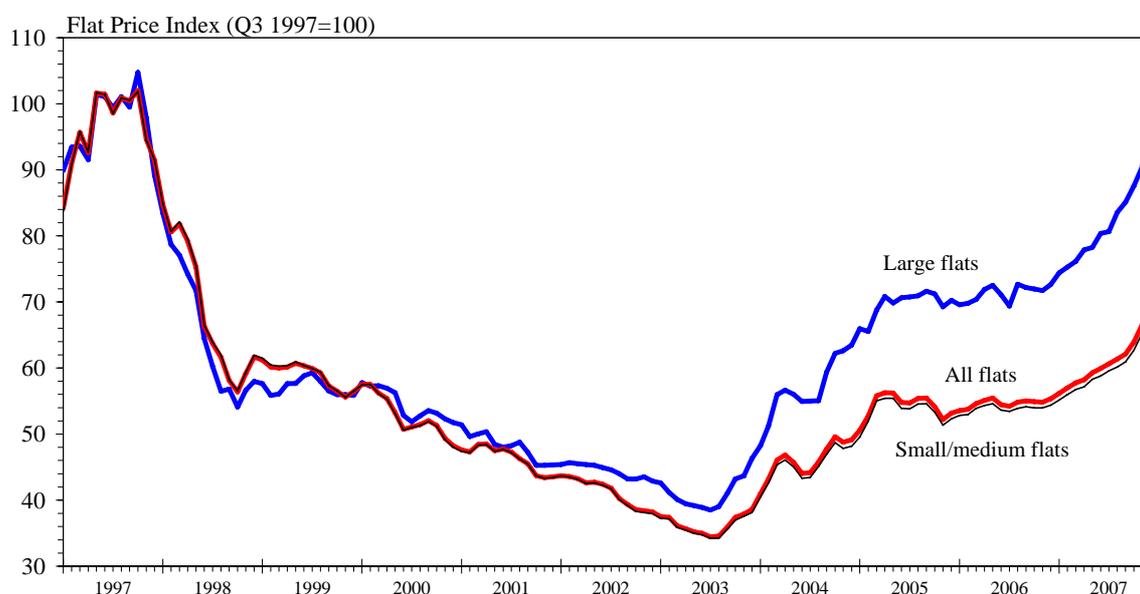
Property

4.1 Having quietened down for more than a year, the *residential property market* turned active again in 2007. Both trading activities and prices picked up over the course of the year, as acquisition interest revived sharply amidst rising income and an improving job market. Market sentiment was particularly upbeat in the fourth quarter, fuelled by successive interest rate cuts totalling one percentage point from September to December, and increasing expectation of

further interest rate easing down the road.

4.2 Overall flat prices rose markedly further by about 11% during the fourth quarter of 2007, giving a cumulative increase of about 24% from end-2006 to end-2007. The full-year price increase for large flats was more pronounced at about 31%, as compared with that of about 24% for small/medium flats. Against the respective peaks in 1997, the average price of large flats was only about 9% lower, but the gap for small/medium flats, which constituted more than 90% of private housing supply, was still substantial at about 34%. Home purchase affordability remained good, as the price increases were well supported by improving household income as well as lower mortgage rates.

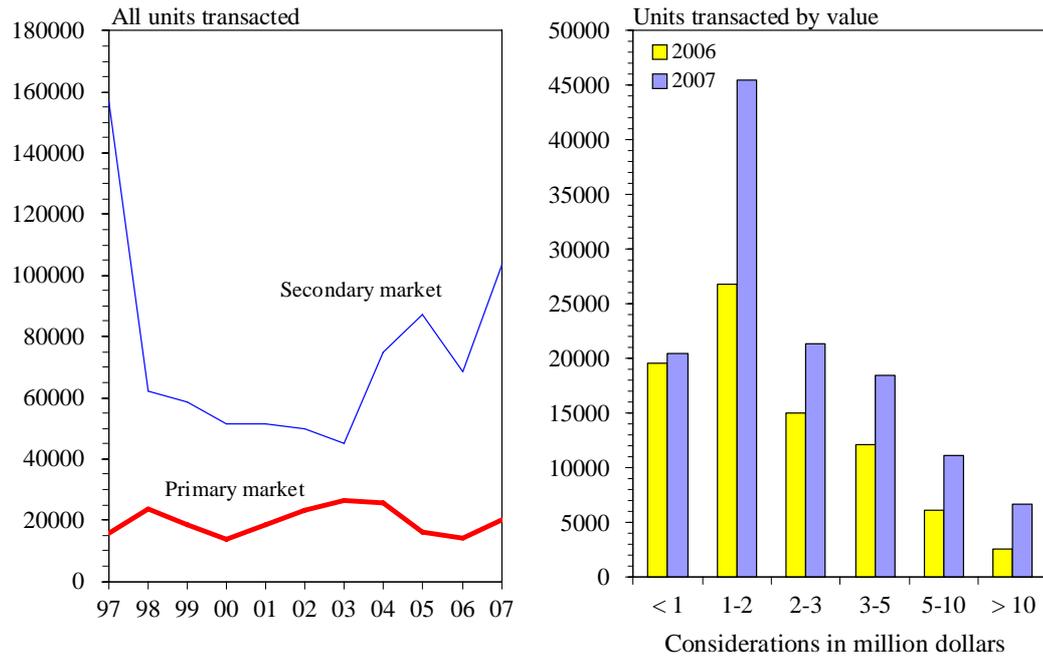
Diagram 4.1 : Flat prices have resumed a distinct increase after the earlier market consolidation



Note : Residential property price index pertains to secondary market transactions only. Large flats refer to those with saleable area of at least 100 m², while small/medium flats refer to those with saleable area of less than 100 m².

4.3 Sales of residential property surged by 50% to a post-1997 high of 123 575 units in 2007. Analyzed by segment, primary and secondary sales leaped by 44% and 51% respectively in 2007, while trading volume rose extensively across different price ranges. The surge in transactions of property worth between \$1 million and \$2 million was particularly distinct, following the stamp duty reduction for this range of consideration in the 2007/08 Budget.

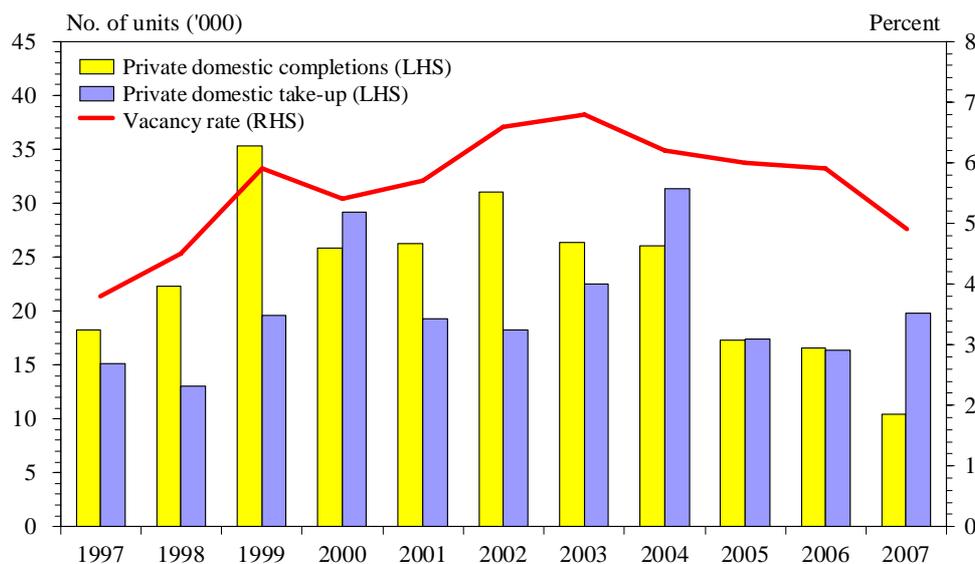
Diagram 4.2 : Housing sales staged a full-fledged rebound in 2007



4.4 Leasing demand for residential property held firm. Overall flat rentals notched up modestly by about 4% during the fourth quarter of 2007, cumulating to an increase of about 15% over end-2006. As the increase was smaller than that of flat prices, the rental yield declined slightly from 4.5% at end-2006 to 4.1% at end-2007.

4.5 The recent upturn of the housing market was largely led by user demand. Reflecting this, take-up⁽¹⁾ of completed residential flats rose strongly by about 21% to 19,846 units in 2007, which considerably exceeded the new completions of 10 471 units in the year, thereby leading to a marked fall in vacancy rate from 5.9% at end-2006 to 4.9% at end-2007. According to the latest forecast, completions will rise back, albeit modestly, to about 11 000 units in 2008 and 12 500 units in 2009. In regard to the potential supply of new private residential flats, it was estimated that the number of unsold completed flats and unsold pre-completed flats already under construction, together with the number of flats on disposed sites where construction was to commence, could make up a total of around 65 000 units in the next few years.

Diagram 4.3 : Rising take-up concurrent with declining vacancy reflected that the recent pick-up in housing sales was primarily user-led

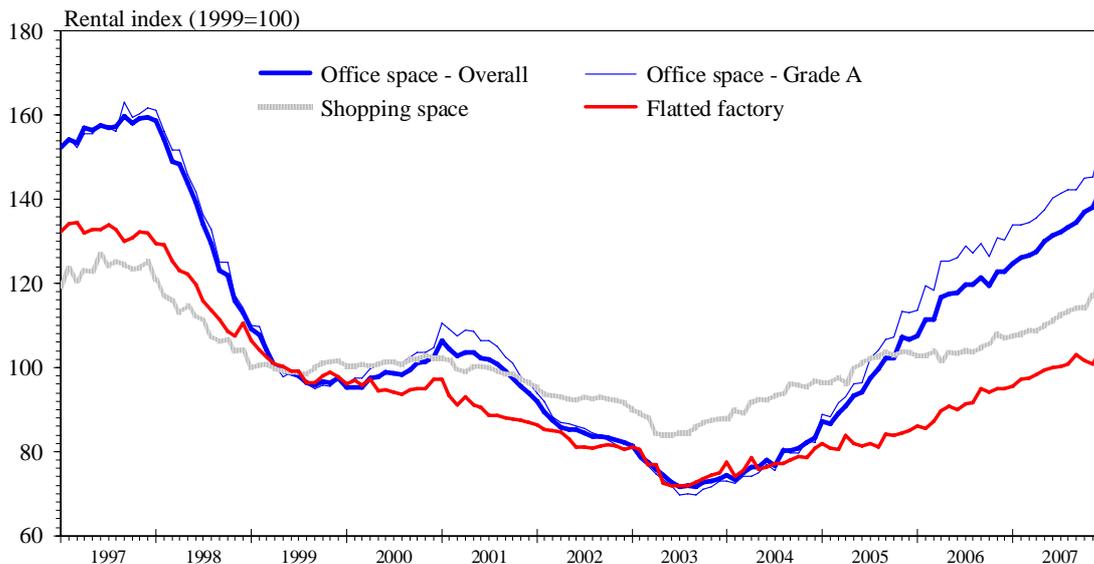


Note : Village houses are included in the figures up to 2001 but excluded in the figures from 2002 onwards.

4.6 The *non-residential property* markets stayed strong in 2007, thanks to the general business upturn. This was particularly obvious in the office market where user demand was hectic across different grades of premises. Compared with end-2006, overall office rentals moved up further by about 15% at end-2007, comprising increases of about 16%, 16% and 11% for office premises in Grade A, B and C respectively. On the back of sanguine leasing prospect and interest rate cuts, sales of office turned more active with transacted prices surging by about 39% in overall terms during 2007.

4.7 As regards shopping and flatted factory spaces, rentals and prices likewise posted further substantial gains. Compared with end-2006, rentals of shopping and flatted factory spaces rose by about 12% and 9% respectively at end-2007. Similar to the situation in the office market, the price gains for shopping and flatted factory spaces were even more notable, at 21% and 29% respectively.

Diagram 4.4 : Hectic leasing demand for commercial and industrial properties alongside extensive pick-up in business activities



4.8 Increased demand has led to a visible fall in vacancy rates of shopping space and flatted factory space, from 9.8% and 7.2% respectively at end-2006 to 8.1% and 6.2% at end-2007. Yet for office space, the vacancy rate rose from 7.7% to 8.9% over the period, as completions of new office space almost tripled to 320 000 m² in 2007. The new supply was concentrated in Grade A premises in non-core districts. The vacancy rate of Grade A office space thus rose markedly in overall terms, from 7.6% at end-2006 to 9.7% at end-2007, but stayed at a very low level in core districts, such as 3.6% in Central and 4.9% in Wanchai/Causeway Bay. Completions of overall office space are forecast to rise further to about 342 000 m² in 2008, of which more than 90% are A-graded premises in non-core districts. This is likely to reinforce the on-going trend of office relocation from core to non-core districts.

Land

4.9 Reflecting developers' increased confidence on the property market outlook, land acquisition through the *Application List* was active throughout the year of 2007. A total of 11 residential sites and one commercial-cum-residential site were successfully triggered from the List and subsequently sold through auction. Market responses were generally favourable, with the prices fetched higher than the trigger prices by 32-147%. The total area and land premium involved were 14.9 hectares and \$32.3 billion respectively in 2007, which exceeded the combined total of the corresponding figures in the preceding two years by 123% and 70%.

4.10 Regarding *lease modifications* on existing developed and developable land and *exchange of land* in the private sector domain, 107 sites totalling 32.8 hectares were approved in 2007, as compared to the corresponding figures of 119 sites and 23.6 hectares in 2006. Within the approvals in 2007, 62 sites totalling 24.1 hectares and 45 sites totalling 8.8 hectares were designated for private residential and non-residential property developments respectively.

Energy

4.11 On 7 January 2008, the Government entered into the post-2008 *Scheme of Control Agreements* with the two power companies. Under the new agreements to be effective on 1 October 2008 and 1 January 2009 respectively, the permitted rate of return of the two power companies will be reduced from the existing 13.5-15% on Average Net Fixed Assets to 9.99%. With the reduced permitted rate of return, basic electricity tariffs of the power companies may be lowered. Besides, a mechanism will be introduced to encourage the power companies to reduce emissions and increase the use of renewable energy⁽²⁾. To pave the way for an open electricity market, the tenure of the new agreements is reduced from the existing 15 years to 10 years. The Government will take into account the market readiness for an open market in deciding whether to extend the new agreements for another five years. The Government will make necessary preparations in the next regulatory period, including studies on open market models and the regulatory framework, as well as enhanced interconnection between the grids of the two power companies.

Transport

4.12 To further consolidate Hong Kong's role as a global city and lay a new foundation for its sustained development, the Government has been striving to develop further Hong Kong's external transport network and internal transport infrastructures. In 2007, the Shenzhen Bay Port and the Sheung Shui to Lok Ma Chau Spur Line have commenced operation. As stated in the Policy Address by the Chief Executive in October 2007, the Government will press ahead with several large-scale transport infrastructures in the coming years.

4.13 On *domestic transport infrastructure projects*, the railway scheme for the West Island Line was gazetted in October 2007. It is expected that the construction work will commence in 2009 for target completion by 2013/2014. At the same time, the Government is pressing ahead with two other new rail

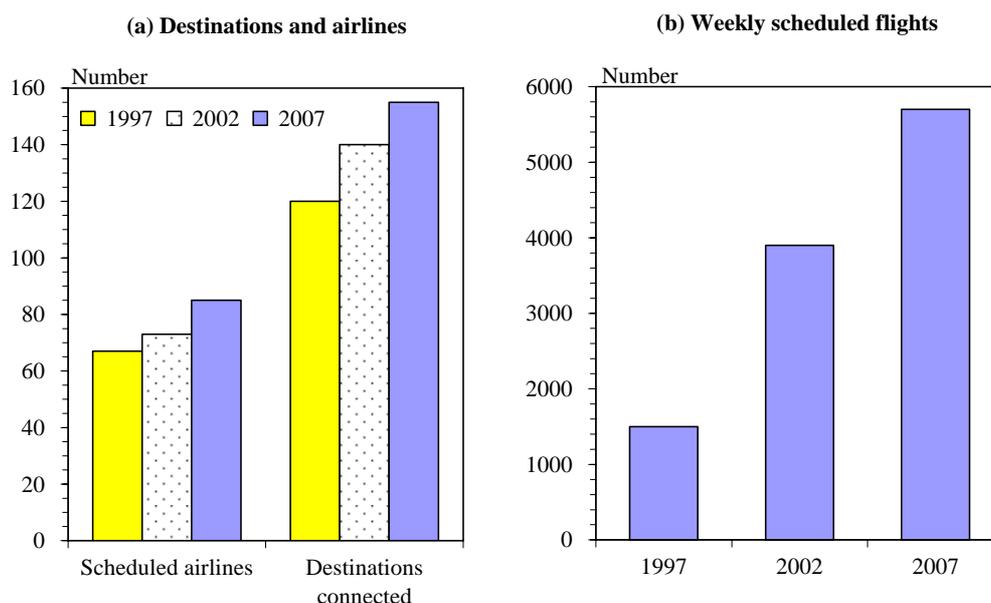
projects, namely the Shatin to Central Link and the South Island Line, which are envisaged to commence construction by around 2010 and 2011 respectively.

4.14 On *cross-boundary transport infrastructure projects*, the Government of the Hong Kong Special Administrative Region has been working closely with the Guangdong Provincial Government and the Government of the Macao Special Administrative Region on the Hong Kong-Zhuhai-Macao Bridge project. So far, more than 20 topical studies under the feasibility study have been completed. The three governments have been pressing ahead with the remaining topical studies and striving for early implementation of the project. As regards the Guangzhou-Shenzhen-Hong Kong Express Rail Link, the Government has decided that a dedicated corridor should be adopted for the Hong Kong Section and is now examining the relevant project proposal. The Rail Link is expected to reduce the rail travel time between Guangzhou and Hong Kong from the present 100 minutes to below 60 minutes.

4.15 As regards the proposed Liantang-Heung Yuen Wai Boundary Control Point, the Hong Kong-Shenzhen Joint Preliminary Planning Study on the project is underway and poised for completion soon. Besides, the internal planning study by the Government of the Hong Kong Special Administrative Region is also targeted for completion in the first quarter of 2008. The findings of both studies and their way forward will be discussed by the newly established Hong Kong-Shenzhen Joint Task Force on Boundary District Development.

4.16 On air transport, the first meeting of the Task Force on Airport Co-operation between Hong Kong and Shenzhen was held on 17 January 2008. As part of the work plan agreed by the two sides, there would be a consultancy study (with target completion within 2008) to look into the feasibility of a rail link between the Hong Kong International Airport and the Shenzhen International Airport, with a view to generating maximum synergy from their comparative advantages. While the Hong Kong International Airport owes its strength to international connectivity, the Shenzhen International Airport is well-linked to many of the cities within the Mainland.

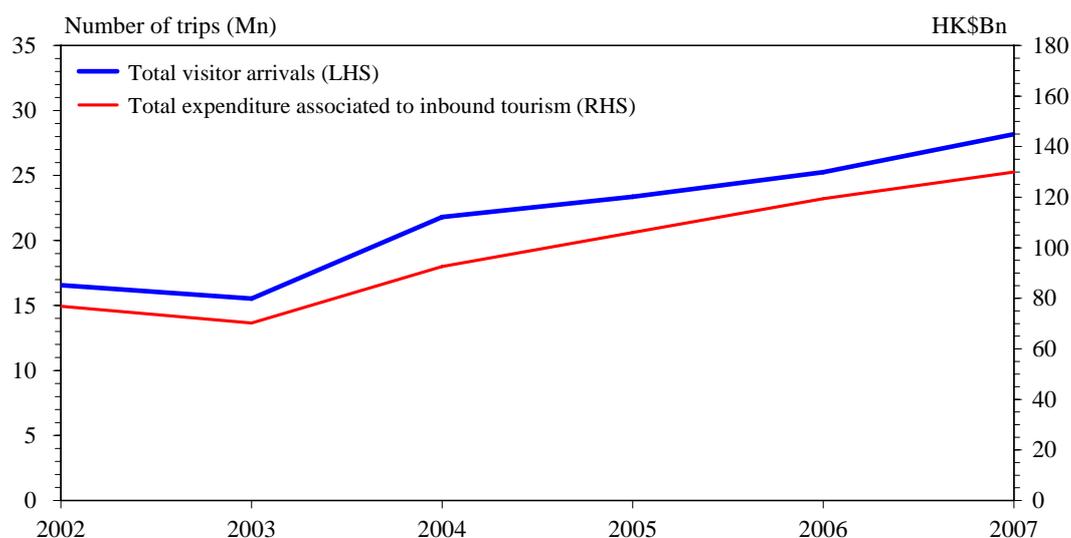
Diagram 4.5 : Hong Kong as an aviation hub has competitive edge in terms of international flight connectivity and service frequency



Tourism

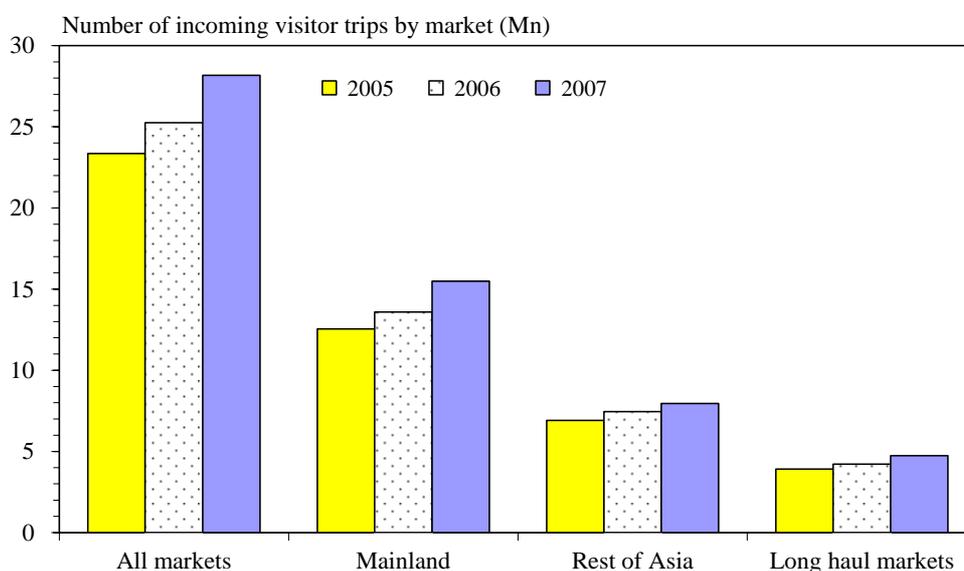
4.17 Inbound tourism remained vibrant in 2007, with the number of *incoming visitors* surging by 11.6% to a new record high of 28.2 million. The growth pace picked up progressively over the course of the year, from 6.8% year-on-year in the first half to 16.0% in the second half. Per capita spending⁽³⁾ of overnight and same-day in-town visitors, respectively taking up 60.9% and 39.1% of visitor arrivals, rose visibly further by about 7.6% and 14.5% to \$5,162 and \$1,162 in 2007. On the back of concurrent growth in visitor trips and per capita visitor spending, the total expenditure associated to inbound tourism⁽⁴⁾ rose from \$119.4 billion in 2006 to about \$130 billion in 2007⁽⁵⁾.

Diagram 4.6 : Both visitor arrivals and tourism expenditure soared to new heights in 2007



4.18 The remarkable visitor growth in 2007 was broadly based across major markets, benefiting from the strong Mainland market as well as an expanding international travel market. The appreciation of renminbi and many other major currencies against Hong Kong dollar was another boosting factor. Arrivals from the Mainland showed a renewed surge of 13.9% in 2007, with the number of arrivals under the Individual Visit Scheme leaping further by 28.8%. Arrivals from other Asian markets rose steadily by 6.8%, while arrivals from long-haul markets showed an accelerated increase of 12.2% in 2007, with the impetus mainly coming from Europe and Middle East.

Diagram 4.7 : Broadly based visitor growth has reinforced the balance of visitors from key markets



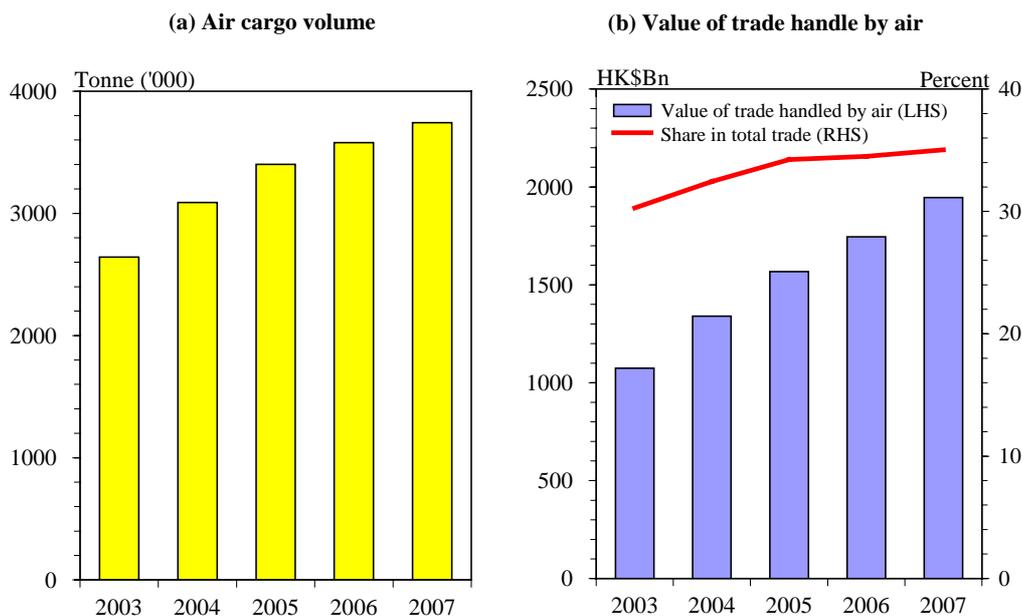
4.19 While a degree of competition always exists between neighbouring tourism cities, this in fact would also present opportunities for developing complementary travel. Guangdong, Macao and Hong Kong have their unique charm and a wide range of attractions and tourism resources that can complement each other. To tap into the market potentials, Hong Kong has been working closely with Guangdong and Macao to step up cooperation in tourism. At the meeting among Tourism Marketing Organisations of Guangdong, Hong Kong and Macao held in December 2007, a number of initiatives were agreed to step up cooperation in overseas promotion of multi-destination travel and training of tourism-related talents.

Logistics

4.20 The logistics sector is an important sector supporting Hong Kong's business and trade growth. Latest indications in 2006 showed that the logistics sector as a whole directly contributed 5% of GDP. Apart from cargo handling, activities of ship-owners and operators of sea-going vessels were also important growth drivers, reflecting the attraction of Hong Kong as an international maritime centre.

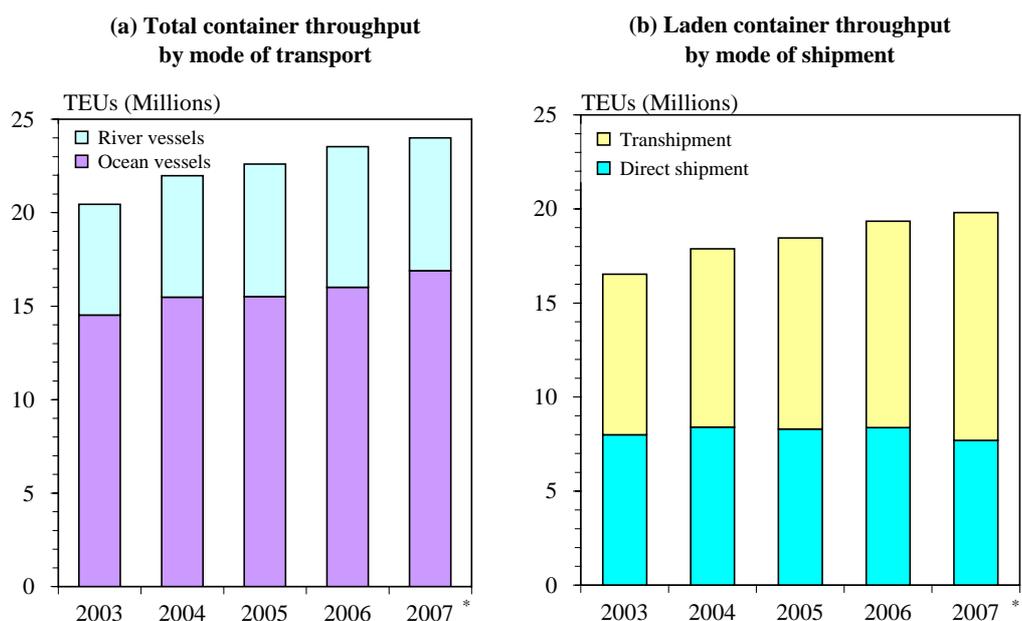
4.21 *Air cargo* movements increased further by 4.5% to 3.7 million tonnes in 2007, though this was slower than the average annual growth of 9.6% from 2002 to 2006. The value of trade (excluding transshipment cargoes) handled by air recorded a faster growth of 11.5% in 2007, conceivably due to a rising share of high-value merchandise in air freight particularly with the Mainland. Of total value of trade (excluding transshipment cargoes), the share handled by air rose to 35% in 2007.

Diagram 4.8 : Air freight maintained a solid growth in recent years



4.22 On *port cargo*, overall container throughput handled by Hong Kong port rose modestly by an estimate of 1.9% to 24 million TEUs in 2007. This came after an increase of 4.1% in 2006. Transshipment continued to lead Hong Kong's container throughput growth, backed by the huge volume of cargoes related to the South China hinterland. Also contributed were Hong Kong's free port status and the frequent shipping schedules that gave an edge in the handling of international transshipment.

Diagram 4.9 : Port container throughput sustained a modest uptrend on the back of further growth in transshipment cargo traffic



Note : (*) Total container throughput for 2007 is the preliminary estimate by Hong Kong Port Development Council. Its breakdowns by mode of transport and the laden container throughput by mode of shipment are crudely estimated from the profile in the first 11 months of 2007.

Innovation and technology

4.23 Hong Kong and the Mainland have been developing deeper and more extensive collaboration in innovation and technology, with a view to generating synergy from the respective strengths to mutual benefit. At the third meeting of the Mainland/Hong Kong Science and Technology Cooperation Committee held on 16 April 2007, the State Ministry of Science and Technology and the then Commerce, Industry and Technology Bureau (CITB) agreed to devise a new mechanism to process applications for setting up state key laboratories in Hong Kong. The local universities have shown keen interest in joining the State Key Laboratories Programme and a total of 17 applications have been received as at December 2007. Besides, CITB and the State Ministry of Information Industry signed an agreement in April 2007 which would facilitate the two sides to strengthen technological cooperation and encourage Hong Kong experts to participate in the formulation of national standards in areas relating to the information industry. In December 2007, the Government agreed with the Guangdong Provincial Government and the Shenzhen Municipality Government to co-fund eight applied research and development projects under the Hong Kong/Guangdong Technology Co-operation Funding Scheme.

4.24 Furthermore, the Government entered into a co-operation agreement on “Shenzhen/Hong Kong Innovation Circle” with the Shenzhen Municipality Government in May 2007. The agreement aimed at comprehensive promotion and enhancement of technology collaboration between Shenzhen and Hong Kong, including exchange of talent and sharing of resources, with a view to upgrading the two places into a region with ample innovation resources and dynamic innovation activities. The first meeting between the two sides was held in October 2007 to discuss various issues which included, *inter alia*, setting up of interactive base in the technology parks of the two sides and reinforcement of intellectual property protection.

4.25 The West Kowloon Cultural District (WKCD) project is a major investment in Hong Kong’s arts and cultural infrastructure. As an integrated cultural hub, WKCD is expected to open up a wealth of new opportunities for investment in arts and cultural activities, thereby stimulating the development of cultural and creative industries in Hong Kong. By supporting arts education and cultural appreciation in the community, the project will also help nurture a pool of creative talents that are necessary for Hong Kong to develop into a creative economy. Taking into account the results of the Public Engagement

exercise that ended in December 2007, the Government has drawn up a bill for establishing the WKCD Authority to take forward the project. The bill will be introduced into the Legislative Council in February 2008.

4.26 Digital terrestrial television (DTT) has been launched since end-December 2007. Apart from enhancing reception quality and coverage, DTT increases the capacity of broadcasting infrastructure for the provision of a variety of communications to meet Hong Kong's future needs as a digital city, and maintain its position as a regional broadcasting hub. Coverage will be raised from half of the population under initial launch to 75% by August 2008. The full implementation of DTT will release spectrum for the development of new multimedia services and enhance Hong Kong's role as a digital city. Subject to further market and technical studies, the Government aims to switch off analogue broadcasting in 2012 the earliest.

Notes :

- (1) Take-up figures in respect of domestic premises represent the net increase in the number of units occupied in the year under review and for non-domestic premises, the net increase in occupied floor space in the year. The figures are derived at by adding the completions in that year to the vacancy figures at the beginning of the year, then subtracting the years' demolition and the year-end vacancy figures. Take-up should not be confused with the sales of new developments, and it bears no direct relationship to the number of units or amount of space sold by developers.
- (2) Under the new Scheme of Control Agreements, the permitted rate of return of the two power companies will be reduced by 0.2 to 0.4 percentage point if they exceed the emission cap for any of the pollutants specified in their Specified Process Licences by the Environmental Protection Department. On the other hand, 0.05 to 0.1 percentage point in the permitted rate of return may be awarded to the companies if their emission in all the pollutants is below the specified caps. In addition, the power companies will enjoy a 11% permitted rate of return for their investment in renewable energy facilities, and a bonus of 0.01 to 0.05 percentage point in the permitted rate of return depending on the extent of renewable energy usage in their electricity generation. A maximum award of 0.02 percentage point in the permitted rate of return will be given based on the number of energy audits the power companies perform for customers and the actual energy saved.
- (3) Per capita visitor spending is derived from the total destination consumption expenditure viz. expenditure on goods and services consumed in Hong Kong, and visitor arrivals (except servicemen, aircrew members and transit/transfer passengers). Expenditure by visitors on cross-boundary transportation services is not covered.

- (4) Latest indications show that about 75% of the total expenditure associated to inbound tourism are destination consumption expenditure by all inbound visitors and travellers for goods and services that they consumed in Hong Kong. The remaining 25% are expenditure by these visitors and travellers on cross-boundary transportation services provided by Hong Kong-based carriers.
- (5) The figures on per capita visitor spending and total expenditure associated to inbound tourism in 2007 are provisional estimates by the Hong Kong Tourism Board.

CHAPTER 5 : THE FINANCIAL SECTOR[#]

Summary

- *Activities in the financial sector were buoyant during 2007, supported by the further financial integration with the Mainland and the growing diversity in products offered in the markets.*
- *The financial system in Hong Kong was by and large unscathed by the global credit market turmoil, thanks to prudent management and the strong regulatory framework. Nevertheless, repercussions of the turmoil have yet to play out fully. Thus close monitoring of the situation is still warranted.*
- *Money supply grew swiftly during 2007, while the negative spread between Hong Kong dollar interbank interest rates and the Euro-dollar deposit rates persisted for most of the year. Ample liquidity and low interest rates provided additional support to the local asset markets and the overall economy.*
- *Given the keen demand for Hong Kong dollar assets, the HKMA conducted market operations to sell Hong Kong dollars against US dollars to banks towards the end of October 2007. However, Hong Kong dollar exchange rate indices weakened steadily during 2007, alongside the slide in US dollar vis-à-vis other major currencies.*
- *2007 was another record year for the local stock market, albeit accompanied with significant volatilities, particularly after the outbreak of the global credit market turmoil. The Hang Seng Index broke through the 30 000 mark in October before easing towards the end of 2007, whilst the market capitalisation ended the year above the \$20 trillion mark.*
- *Amidst the intense competition globally, participants in the local financial markets continued to strive for innovative products to satisfy their customers' ever-changing demand. By adhering to the principle of "Big Market, Small Government," regulatory authorities would continue to provide a sound regulatory environment that is at the same time conducive to financial innovations and encourages greater product variety.*

(#) **This chapter is jointly prepared by the Hong Kong Monetary Authority (HKMA) and the Economic Analysis Division.**

Overall situation

5.1 The financial sector continued to perform vibrantly in 2007, under a strong economic backdrop in both the Mainland and Hong Kong. Benefiting from abundant inflow of capital and interest rate cuts in the US during the second half, local interest rates remained at accommodative levels, further underpinning the strength in the investment markets and the economy as a whole. However, continuing financial turbulence would likely remain one of the key factors affecting the performance of Hong Kong's financial sector in the near term.

5.2 The local banking system has been unharmed by the global financial market turbulence that started in the summer of 2007, given the limited direct exposures to US subprime mortgage investments for most of the local financial institutions. The sound institutions and regulatory framework will enable Hong Kong's financial system to withstand the external shocks.

5.3 Hong Kong's position as a leading international financial centre in the region has been firmly supported by further integration with the Mainland. Market participants and the Government will continue to push for innovations in the market to build a diversified financial market. The issuance of renminbi-denominated bonds in 2007 was well-received by the market, and efforts to attract more listing of overseas enterprises and develop an Islamic finance market in Hong Kong are some other initiatives to enrich the breadth of product offerings and enhance the city's competitive edge.

Interest rates and exchange rates

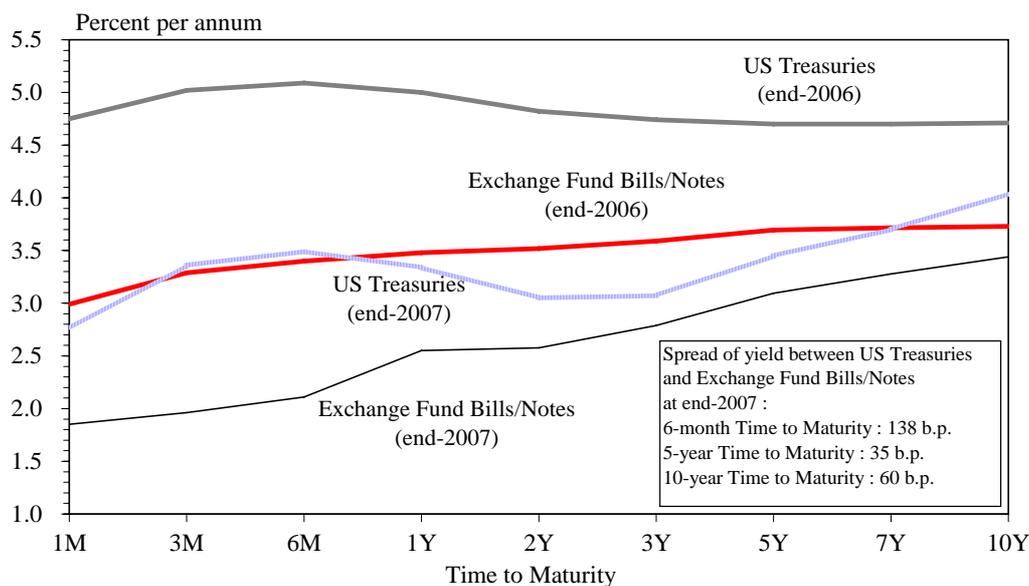
5.4 Throughout 2007, *Hong Kong dollar interbank interest rates* largely tracked their US dollar counterparts. Between January and August, short-term Hong Kong Interbank Offered Rates (HIBORs) were generally on a steady up-trend, first as a result of interest rate arbitrage activities and then because of increased liquidity demand arising from concerns about the contagion effect of the US sub-prime mortgage problem. The 50-basis point cut in the US Federal Funds Target Rate on 18 September resulted in brief decline in HIBORs, but funding demand associated with *initial public offerings (IPOs)* of Mainland companies drove up the rates again. The one-month and three-month HIBORs reached their highest levels in 2007 of 5.64% and 5.39% on 12 October, leading to a short period of positive interest spreads between HIBORs and the corresponding US-dollar interest rates. Yet, from mid-October, interbank interest rates eased again, because of the expectations of further monetary

easing in the US, and subsequently due to the increased supply of funds in the interbank market after the triggering of the strong-side *Convertibility Undertaking* of 7.75 in late October.

5.5 Large write-offs for sub-prime-related debt securities and huge quarterly losses reported by a number of large US financial institutions in November have led to a brief rebound in both US dollar and Hong Kong dollar short-term interest rates, but further monetary easing from the US and other major central banks afterwards resulted in decreases in short-term HIBORs towards year-end. The one-month and three-month HIBORs closed at 3.13% and 3.31% respectively at end-2007, compared with 3.88% and 3.84% respectively at end-2006. The discount of three-month HIBOR over the corresponding Euro-dollar deposit rate was 144 basis points at end-2007, compared with 150 basis points at end-2006.

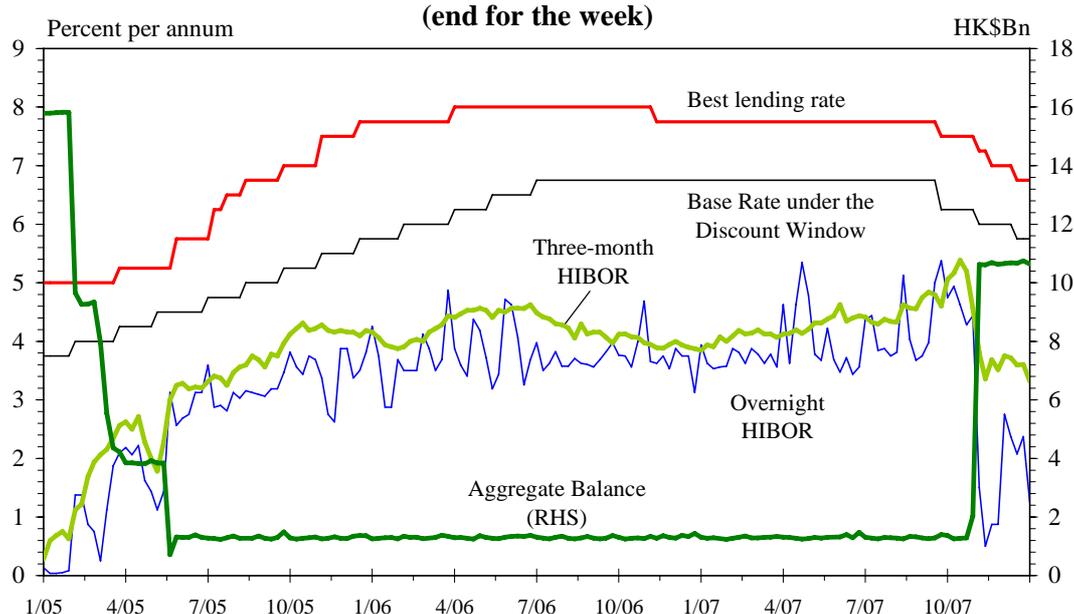
5.6 With the easing of monetary policy in the US, the *Hong Kong dollar yield curve* shifted downward in 2007. In the fourth quarter of 2007, the yields for short-dated Exchange Fund Bills declined to very low levels, partly reflecting the strong demand for these papers for settlement purposes alongside the increase in equity market transactions. However, Discount Window activities remained normal. The overnight interbank interest rate did not exceed the *Base Rate* under the Discount Window operated by the HKMA, even though the Base Rate was reduced three times by a total of 100 basis points to 5.75% in December according to an established formula⁽¹⁾. Moreover, there were no signs of stress in the local credit markets in the wake of the US sub-prime mortgage problem. For the year as a whole, interest rate spread between 10-year Exchange Fund Notes and US Treasuries of the same maturity narrowed from 98 basis points at end-2006 to 60 basis points at end-2007, due to the notable decline in US rates across all maturities.

Diagram 5.1 : Hong Kong dollar yield curve shifted downward amidst monetary easing in the US



5.7 At the retail level, banks cut their best lending rates and savings deposit rates four times between September and December 2007, each time by 25 basis points. The two best lending rates in the market declined from 7.75-8.00% at end-2006 to 6.75-7.00% at end-2007, and the average interest rate for savings deposits quoted by major banks decreased as well, to 1.35% in December 2007 compared with 2.27% in December 2006. The composite interest rate⁽²⁾, which indicated the average cost of funds for banks, also declined to 2.29% at end-2007, from 2.86% a year ago. Reflecting keen competition in the mortgage market, the proportion of newly approved loans priced at more than 2.5% below the best lending rate rose from 61.0% in December 2006 to 87.9% in December 2007. Combined with the lowered interest rates and rise in inflation, the cost of home financing decreased in real terms.

Diagram 5.2 : Hong Kong dollar interest rates fell towards year-end given abundant liquidity
(end for the week)



5.8 The Hong Kong dollar exchange rate against the US dollar mostly stayed on the weak side between January and early-August, with the Hong Kong dollar exchange rate reaching a peak of 7.829 per US dollar in early August, reflecting interest rate arbitrage activities and the conversion of proceeds from IPOs into US dollars by newly-listed Mainland companies. However, the exchange rate began to strengthen afterwards, due partly to equity-related demand and partly to the general weakness in the US dollar. Taking into account market conditions, the HKMA operated within the Convertibility Zone of 7.75 to 7.85 to sell Hong Kong dollars on 23 October. Subsequently, the strong-side Convertibility Undertaking was triggered on 26 October and 31 October, prompting the HKMA to passively sell Hong Kong dollars to banks. Consequently, the Aggregate Balance increased to around HK\$10.6 billion in early November. These operations softened both the Hong Kong dollar exchange rate and interbank interest rates, normalising the relationship between a strong exchange rate and tight interbank interest rates observed before.

5.9 In the last two months of 2007, the Hong Kong dollar spot exchange rate depreciated towards the centre of the Convertibility Zone and closed at 7.802 on 31 December, reflecting carry trades in a low interbank interest rate environment. For the year as a whole, while the Hong Kong dollar nominal exchange rate against the US dollar stayed within the Convertibility Zone, the trade-weighted *Hong Kong dollar Nominal and Real Effective Exchange Rate Indices*⁽³⁾ declined by 5.3% and 5.9% respectively due to the weakness in US

dollars against other major currencies, including the renminbi. Except a short-lived episode of small premiums in mid-October, the *Hong Kong dollar forward points* were generally negative. For the year as a whole, the three-month and 12-month forward discounts narrowed from -278 and -977 pips (each pip is equivalent to HK\$0.0001) respectively at end-2006, to -260 and -660 pips at end-2007.

Diagram 5.3 : Forward spread remained wide for most of 2007 (end for the week)

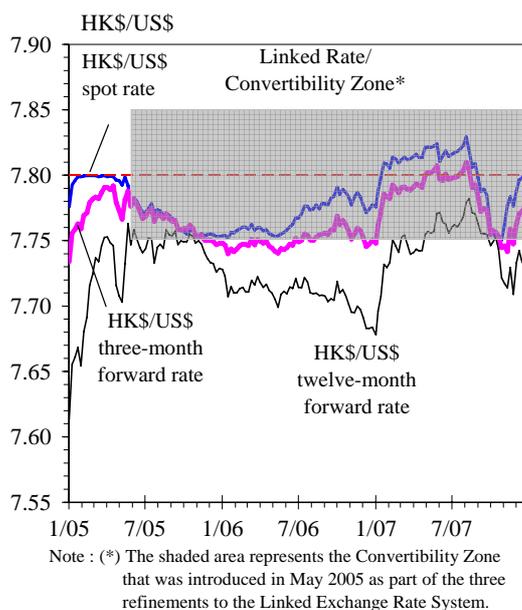
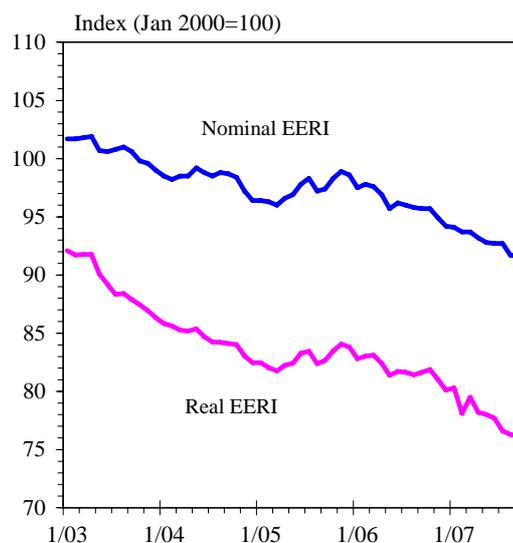


Diagram 5.4 : Trade-weighted EERI continued to trend downward amidst a weak US dollar (average for the month)



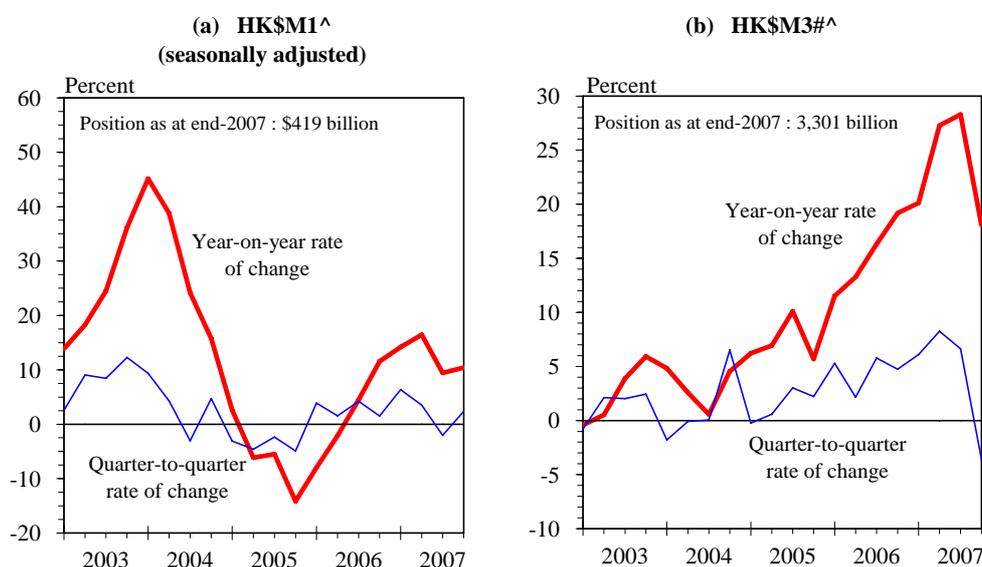
Money supply and banking sector

5.10 Monetary aggregates grew at a brisk pace in 2007. The seasonally adjusted Hong Kong dollar narrow *money supply* (HK\$M1)⁽⁴⁾ rose by 2.4% in the fourth quarter over the previous quarter. For the year as a whole, it expanded by 10.4% following an increase of 11.5% in 2006. The marked expansion was largely attributable to strong economic growth, buoyant fund-raising activities and increased turnover in the stock market. Hong Kong dollar broad money supply (HK\$M3) continued to rise alongside economic expansion. While it shrank by 3.6% in the fourth quarter over the third quarter partly owing to a high base of comparison due to IPOs, it rose by 18.1% for the whole year of 2007.

5.11 *Total deposits* with authorised institutions (AIs)⁽⁵⁾ expanded by 23.4% year-on-year to \$5,869 billion (comprising Hong Kong dollar deposits of \$3,075 billion and foreign currency deposits of \$2,794 billion) at end-2007, as financial positions of both the household and corporate sectors further strengthened amid

sustained improvement in labour market, a robust economy and buoyant asset markets.

Diagram 5.5 : Money supply grew strongly amidst strengthening household and corporate financial positions



Notes : (^) Figures refer to the positions at end of quarter.
(#) Adjusted to include foreign currency swap deposits.

5.12 *Total loans and advances* increased by 20.0% year-on-year to \$2,962 billion (comprising Hong Kong dollar loans of \$2,185 billion and foreign currency loans of \$777 billion) at end-2007 along with brisk business expansion. Analysed by economic sectors, loans to stockbrokers registered the highest growth, reflecting vibrant stock market activities. Growth in loans for property development and investments, trade financing and financial concerns also picked up in 2007. The outstanding stock of residential mortgage loans increased during the year, helped by the rise in residential property transactions in the market especially in the fourth quarter. As growth in Hong Kong dollar loans was lower than that in deposits, the Hong Kong dollar loan-to-deposit ratio declined from 74.7% at end-2006 to 71.0% at end-2007, suggesting abundant liquidity in the banking system and a prudent approach to credit quality by individual banks.

Table 5.1 : Loans and advances

All loans and advances for use in Hong Kong											
Loans to :											
% change during the quarter		Finance trade	Manu- facturing sector	Whole- sale and retail trade	Building, construction, property development and investment	Purchase of residential property ^(a)	Financial concerns	Stock-brokers	Total ^(b)	All loans and advances for use outside Hong Kong ^(c)	Total loans and advances
2006	Q1	-2.4	-1.9	0.9	0.6	-1.1	3.6	5.3	-0.3	9.1	0.7
	Q2	10.1	3.7	1.9	5.7	-0.6	-1.3	-6.0	2.8	12.0	3.9
	Q3	4.9	-5.4	0.1	-0.9	-0.5	-0.1	675.2	1.5	16.7	3.3
	Q4	-4.7	-2.7	2.1	4.0	0.3	2.2	-83.7	-1.4	-0.2	-1.2
2007	Q1	-1.0	3.5	1.9	1.0	-0.1	5.9	994.1	7.6	12.3	8.3
	Q2	12.2	7.4	4.0	6.1	1.2	10.2	39.5	6.4	10.7	7.0
	Q3	4.2	4.8	1.8	5.7	1.4	6.2	11.9	5.8	9.9	6.4
	Q4	4.1	2.5	3.1	4.2	2.2	9.6	-86.4	-4.4	7.2	-2.6
Total amount at end-2007 (\$Bn)		183	122	117	578	623	251	19	2,460	502	2,962
% change over a year earlier		20.4	19.5	11.3	18.1	4.7	35.8	125.4	15.7	46.9	20.0

- Notes :
- (a) Figures also include loans for the purchase of flats under the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme, in addition to those for the purchase of private residential flats.
 - (b) Loans to individual sectors may not add up to all loans and advances for use in Hong Kong, as some sectors are not included in this table.
 - (c) Also includes loans where the place of use is not known.

5.13 With solid economic expansion, asset quality of the local banking sector improved further over the course of 2007. The ratio of classified loans to total loans of retail banks dropped further from 1.11% at end-December 2006 to 0.89% at end-September 2007. Over the same period, the arrears for over three months in credit card repayment edged down from 0.37% to 0.36%. The delinquency ratio for *residential mortgage loans* decreased to 0.11% at end-2007 from 0.20% a year ago.

Table 5.2 : Asset quality of retail banks^(a)

(as % of total loans)

<u>As at the end of</u>	<u>Pass loans</u>	<u>Special mention loans</u>	<u>Classified loans</u> (gross)
2006 Q1	95.97	2.71	1.32
Q2	96.15	2.55	1.29
Q3	96.44	2.37	1.19
Q4	96.65	2.24	1.11
2007 Q1	97.11	1.89	1.00
Q2	97.37	1.73	0.90
Q3	97.47	1.64	0.89

Notes : Due to rounding, figures may not add up to 100.

- (a) Period-end figures relate to Hong Kong offices and overseas branches. Loans and advances are classified into the following categories: Pass, Special Mention, Substandard, Doubtful and Loss. Loans in the substandard, doubtful and loss categories are collectively known as “classified loans”.

5.14 Hong Kong implemented the new *Basel II capital adequacy framework* for banks on 1 January 2007. This followed the passage of the Banking (Capital) Rules and the Banking (Disclosure) Rules in November 2006 prescribing how the capital adequacy ratio (CAR) of Hong Kong incorporated AIs shall be calculated and what information on the state of affairs, profit and loss and CAR shall be publicly disclosed. Under the new framework, the CAR for local banks remained stable, averaging 13.5% in the first three quarters of 2007. All individual AIs’ CARs were above the statutory minimum ratios they are required to meet under the Banking Ordinance.

5.15 The implementation of the new framework aligns regulatory capital requirement more closely with the inherent risks of banks, and encourages banks to improve their internal risk management. Adopting the latest international banking standards in this respect will contribute to the safety and soundness of the banking system in Hong Kong and help strengthen the position of Hong Kong as a leading international financial centre.

5.16 Since February 2004, banks in Hong Kong have been offering renminbi services to customers including deposit taking, currency exchange and remittance. At end-2007, a total of 37 licensed banks conducted renminbi banking business in Hong Kong. In 2007, *renminbi deposits* represented about 1% of total foreign currency deposits in Hong Kong, with an outstanding size of about RMB 33 billion yuan at the end of the year.

Table 5.3 : Renminbi deposits in licensed banks

<u>As at end of</u>		Demand and savings deposits (RMB Mn)	<u>Time deposits</u> (RMB Mn)	<u>Total deposits</u> (RMB Mn)	<u>Interest rates on^(a)</u>		Number of licensed banks engaged in RMB business
					<u>Saving deposits^(b)</u> (%)	<u>Three-month time deposits^(b)</u> (%)	
2006	Q1	10,682	11,776	22,458	0.46	0.65	39
	Q2	11,285	11,427	22,712	0.46	0.65	39
	Q3	11,355	11,264	22,619	0.46	0.65	40
	Q4	12,228	11,175	23,403	0.46	0.65	38
2007	Q1	13,643	11,595	25,238	0.46	0.65	38
	Q2	17,228	10,391	27,618	0.46	0.65	38
	Q3	18,458	9,045	27,503	0.46	0.65	37
	Q4	22,539	10,861	33,400	0.46	0.65	37

Notes : (a) The interest rates are sourced from a survey conducted by the HKMA.

(b) Period average figures.

The debt market

5.17 To strengthen Hong Kong's position as an international financial centre, the Government has pushed ahead the growth in Hong Kong's debt market both in size and in depth, by facilitating the introduction of new instruments and enhancing market liquidity. Over the past decade, the outstanding amount in the Hong Kong dollar debt market has increased significantly. In 2007, gross issuance of Hong Kong dollar debt securities amounted to HK\$445 billion. The outstanding size grew by 2% to \$764 billion at the end of the year⁽⁶⁾. This was equivalent to 23% of HK\$M3 or 19% of Hong Kong dollar denominated assets of the entire banking sector⁽⁷⁾. Around 73% of the outstanding debts were issued by the private sector and Multilateral Development Banks, while the remaining were issued by the public sector, including the Exchange Fund papers and debt securities issued by the Government and statutory bodies. In August 2007, the HKMA launched the first issue of 15-year Exchange Fund Notes, extending the benchmark yield curve to 15 years. This marked a key step in the development of the Hong Kong dollar debt market.

5.18 Over the medium to longer term, the Government aims at developing the domestic bond market as a fund raising avenue for enterprises and statutory bodies from the Mainland and other regional economies. The inaugural RMB-denominated bonds in Hong Kong were launched in June 2007. In total, RMB10 billion worth of RMB-denominated bonds were issued in 2007. Developing an Islamic bond market, which was highlighted by the Policy

Address delivered by the Chief Executive in October 2007, is another important initiative to further enrich the product offerings in Hong Kong's financial markets.

Table 5.4 : New issuance and outstanding value of HK dollar debt securities (\$Bn)

		Exchange Fund paper	Statutory bodies/govern ment-owned corporations	Govern- ment	Public sector total	AIs ^(a)	Local corporates	Non-MDBs overseas borrowers ^(b)	Private sector total	MDBs ^(b)	Total
New Issuance											
2006	Annual	220.5	17.4	-	237.9	44.9	21.3	147.0	213.2	3.0	454.1
	Q1	54.4	6.9	-	61.3	14.1	7.0	35.6	56.7	0.2	118.2
	Q2	55.6	3.5	-	59.1	12.0	1.2	42.0	55.2	-	114.3
	Q3	54.1	2.6	-	56.7	10.0	7.0	35.5	52.5	1.8	111.0
	Q4	56.4	4.4	-	60.8	8.8	6.1	33.9	48.8	1.0	110.6
2007	Annual	223.5	19.4	-	242.9	50.8	18.7	130.7	200.2	1.7	444.8
	Q1	55.0	4.0	-	59.0	13.3	5.4	37.9	56.6	1.5	117.1
	Q2	56.9	6.9	-	63.8	20.2	6.5	40.9	67.6	-	131.4
	Q3	56.1	1.5	-	57.6	6.7	5.7	18.7	31.1	-	88.7
	Q4	55.4	7.0	-	62.5	10.6	1.1	33.2	44.9	0.2	107.6
Outstanding (period-end figures)											
2006	Q1	127.9	59.3	10.3	197.5	154.3	44.7	270.0	469.0	17.5	684.0
	Q2	129.3	54.0	10.3	193.6	152.9	43.3	295.3	491.5	17.1	702.2
	Q3	130.4	54.1	7.7	192.2	151.7	48.0	312.5	512.2	18.5	722.9
	Q4	131.8	56.9	7.7	196.4	147.4	52.4	332.4	532.2	19.5	748.1
2007	Q1	133.0	54.6	7.7	195.3	147.7	54.3	335.3	537.3	16.5	749.1
	Q2	134.4	58.0	7.7	200.1	151.6	58.9	350.5	561.0	14.4	775.5
	Q3	135.6	57.2	7.7	200.5	140.7	62.9	338.9	542.4	13.4	756.3
	Q4	136.6	58.5	7.7	202.8	137.5	60.6	350.1	548.2	13.2	764.2

Notes : Figures may not add up to the corresponding totals due to rounding.

(a) AIs : Authorised Institutions.

(b) MDBs : Multilateral Development Banks.

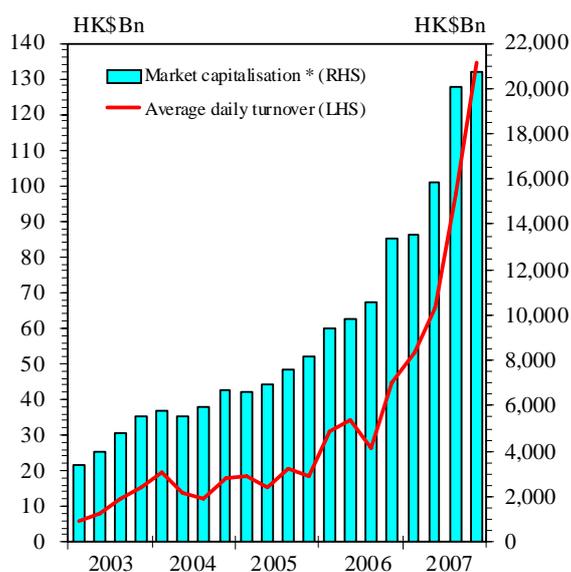
5.19 In July 2007, Fitch upgraded Hong Kong's long-term foreign-currency sovereign rating from "AA-" to "AA," attributing the upgrade to Hong Kong's "robust external financial position, continued improvements in public finances," and "the credible linked exchange rate system." This was followed by Moody's raising the Hong Kong Government's long-term foreign- and domestic-currency bond ratings from "Aa3" to "Aa2" with "Stable" outlook, and Standard & Poor's revising Hong Kong's ratings outlook from "Stable" to "Positive."⁽⁸⁾ The above development reflects wide recognition for Hong Kong's strong economic fundamentals and improving public finance, and would help to lower the borrowing costs for Hong Kong companies, creating a favourable environment for economic expansion.

The stock and derivatives markets

5.20 The *local stock market* fared strongly for 2007 as a whole, setting a number of records in trading activities. Under massive capital inflows and upbeat economic fundamentals in the Mainland and Hong Kong economies, the market was able to rebound robustly after the global stock malaise in mid-August that was triggered by concerns on US subprime mortgages. The *Hang Seng Index (HSI)* and *daily market turnover* registered their all-time highs in October, at 31 638 on 30 October and \$210.5 billion on 3 October respectively. Although stock prices and trading cooled somewhat in November and December, the HSI still managed to close at 27 813 at end-2007, representing a brilliant 39% gain from the end-2006 level, which out-performed the stock markets in major advanced economies. Moreover, the average daily turnover for 2007 rose by an even more impressive 160% from a year earlier to record high of \$88.1 billion.

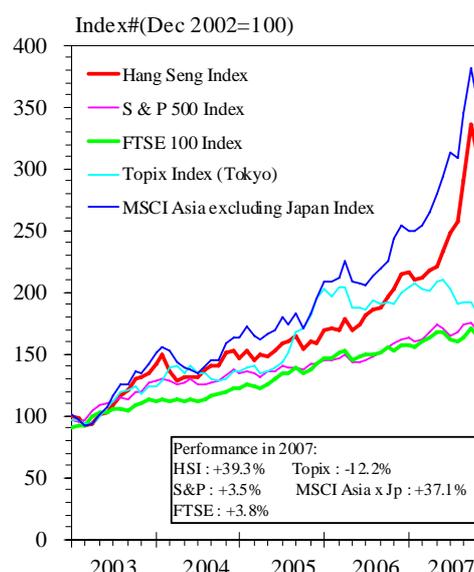
5.21 In tandem with the stock price movements, *market capitalisation* surged to as high as \$23.2 trillion in October and eased to \$20.7 trillion at end-2007 (comprising \$20.5 trillion in the Main Board and \$161 billion in the Growth Enterprise Market (GEM)), but still up by 55% from a year earlier. According to the *World Federation of Exchanges*⁽⁹⁾, at end-2007, the Hong Kong stock market was the seventh largest in the world and third largest in Asia in terms of market capitalisation. In 2007, equity capital raised through new share flotations and post-listing in the Main Board and the GEM amounted to \$558 billion⁽¹⁰⁾, 10% higher than the figure in 2006 in spite of lacking mega IPOs likewise of Industrial and Commercial Bank of China and Bank of China. In addition, total value of equity raised through IPOs of new stocks in 2007 still ranked fourth internationally and second in Asia.

Diagram 5.6 : Buoyant activities in the Hong Kong stock market



Note : (*) Position at end of quarter.

Diagram 5.7 : HSI rose markedly in 2007, out-performing stock markets in developed markets



Note : (#) Position at end of month.

5.22 Hong Kong remained a major fund-raising centre for the Mainland enterprises and the market of choice for international investors to participate in the burgeoning growth in the Mainland economy. In 2007, the Mainland enterprises raised a total of \$362 billion from the Hong Kong stock market, taking up 65% of the total equity raised during the period. Since January 1993, \$1,850 billion of capital had been raised by Mainland enterprises in the Hong Kong stock market, accounting for 57% of the total funds raised. At end-2007, there were 439 Mainland enterprises (including 146 H-share companies, 93 “Red Chips” companies and 200 private enterprises) listed on the Hong Kong stock market, accounting for 35% of the total number of listed companies. The market capitalisation of these Mainland enterprises surged almost 80% during 2007 and reached \$12.0 trillion, which is equivalent to 58% of the total market capitalisation of the Hong Kong stock market. In 2007, 69% of equity turnover in the stock market was contributed by trading of the above Mainland-related stocks.

5.23 The *derivatives market* also enjoyed a year of frantic trading in 2007, especially during the second half. Total trading volume in futures and options contracts⁽¹¹⁾ in 2007 increased by 106% from a year earlier. Among the more popular derivative contracts, the rise in volume is particularly distinct in stock options and H-share index futures, which rose by 155% and 123% respectively. Trading in derivative warrants also recorded a spectacular surge in 2007, with average daily trading value increasing by 163% from 2006’s level, to

HK\$19.1 billion and accounting for about 22% of total securities turnover in the market.

Table 5.5 : Average daily turnover of derivatives contracts of the Hong Kong stock market

		Hang Seng Index Futures	Hang Seng Index Options	H-shares Index Futures	Stock Options	Total Futures and Options traded ^(a)	Derivative Warrants (\$Mn)
2006	Annual	51 491	16 582	19 759	73 390	173 708	7,247
	Q1	46 638	14 287	17 436	61 863	149 618	6,080
	Q2	54 535	17 141	22 703	65 038	172 719	6,354
	Q3	50 281	16 671	16 670	66 836	162 747	6,758
	Q4	54 770	18 278	22 564	100 169	210 829	9,818
2007	Annual	69 760	30 407	44 091	186 923	357 665	19,081
	Q1	61 184	30 495	31 059	124 662	268 878	10,837
	Q2	62 301	31 774	34 783	137 742	285 315	11,662
	Q3	76 286	37 952	54 210	240 131	438 005	18,810
	Q4	78 803	21 353	55 698	241 918	433 668	34,659
	% change in 2007 Q4 over 2006 Q4	43.9	16.8	146.8	141.5	105.7	253.0
	% change in 2007 average over 2006 average	35.5	83.4	123.1	154.7	105.9	163.3

Note : (a) Turnover figures for individual futures and options do not add up to the total futures and options traded as data for some products is not included in this table.

Fund management and investment funds

5.24 In 2007, gross retail sales of *mutual funds*⁽¹²⁾ amounted to US\$45.5 billion, increasing markedly from US\$24.3 billion in 2006. After deducting redemptions, net sales amounted to US\$6.9 billion for 2007 as a whole, compared with US\$3.8 billion in 2006. The rosy figures were mostly driven by sales of equity funds. Funds managed under the *MPF schemes* continued to grow notably in 2007, thanks partly to decent investment return. The aggregate net asset value of the approved constituent funds rose to \$265 billion at end-2007, from \$202 billion at end-2006⁽¹³⁾. Development in retail hedge funds market continued in 2007 as well⁽¹⁴⁾.

5.25 In response to customers' demand for more diversity in wealth management products, financial institutions in Hong Kong continue to strive to

create more variety in their product offerings. For instance, in light of the burgeoning demand for Islamic financial services globally, a local bank launched the first SFC-authorized Islamic fund in November 2007. In order to maintain Hong Kong's position as a leading financial centre in the region, the Government will provide an environment that nurtures financial innovations while ensuring the soundness of the regulatory framework.

Insurance sector

5.26 The *insurance sector* continued to benefit from the demand driven by increased awareness on financial planning and improved financial positions of households. Gross premium income from new long-term business jumped 87.3% in the third quarter of 2007 over a year earlier⁽¹⁵⁾, thanks largely to the strong sales of investment-linked policies, which are gaining popularity among policyholders amidst the solid performance in investment markets generally in the past few years. Premium for general business, on the other hand, showed a small decline of 0.6% in the third quarter of 2007 from a year earlier.

Table 5.6 : Insurance business in Hong Kong (\$Mn)

		<u>General business :</u>				<u>Premium for long-term business* :</u>				
		Gross premium	Net premium	Underwriting profit	Individual life and annuity (non-linked)	Individual life and annuity (linked)	Other individual business	Non-retirement scheme group business	All long-term business	Gross premium from long-term business and general business
2006	Annual	22,958	16,198	2,067	20,928	32,128	203	159	53,418	76,376
	Q1	6,795	4,881	637	4,868	7,284	37	52	12,241	19,036
	Q2	5,337	3,951	723	5,360	9,195	41	38	14,634	19,971
	Q3	5,894	4,024	674	4,792	6,630	58	45	11,525	17,419
	Q4	4,932	3,342	33	5,908	9,019	67	24	15,018	19,950
2007	Q1	6,792	4,904	441	5,982	10,122	62	45	16,211	23,003
	Q2	6,156	4,451	598	3,307	13,189	62	50	16,608	22,764
	Q3	5,861	4,122	744	5,028	16,445	76	40	21,589	27,450
	% change over a year earlier	-0.6	2.4	10.4	4.9	148.0	31.0	-11.1	87.3	57.6

Note : (*) Figures refer to new businesses only. Retirement scheme businesses are excluded.

Notes :

- (1) At present, the Base Rate is set at either 150 basis points above the prevailing US Fed Funds Target Rate or the average of the five-day moving averages of the overnight and one- month HIBORs, whichever is higher.
- (2) In December 2005, the HKMA published a new data series on composite interest rate, reflecting movement in various deposit rates, interbank and other interest rates to closely track the average costs of funds of banks. The published data enable the banks to keep track of changes in funding cost and thus help improve interest rate risk management in the banking sector.
- (3) The trade-weighted Nominal Effective Exchange Rate Index (EERI) is an indicator of the overall exchange value of the Hong Kong dollar against a fixed basket of other currencies. Specifically, it is a weighted average of the exchange rates of the Hong Kong dollar against some 14 currencies of its major trading partners, with the weights adopted being the respective shares of these trading partners in the total value of merchandise trade for Hong Kong during 1999 and 2000.

The Real EERI of the Hong Kong dollar is obtained by adjusting the Nominal EERI for relative movements in the seasonally adjusted consumer price indices of the respective trading partners.

- (4) The various definitions of the money supply are as follows:

M1 : notes and coins with the public, plus customers' demand deposits with licensed banks.

M2 : M1 plus customers' savings and time deposits with licensed banks, plus negotiable certificates of deposit (NCDs) issued by licensed banks, held outside the monetary sector as well as short-term Exchange Fund placements of less than one month.

M3 : M2 plus customers' deposits with restricted licence banks and deposit-taking companies, plus NCDs issued by such institutions and held outside the monetary sector.

Among the various monetary aggregates, more apparent seasonal patterns are found in HK\$M1, currency held by the public, and demand deposits.

- (5) Authorised institutions include licensed banks, restricted licence banks and deposit-taking companies. At end-2007, there are 142 licensed banks, 29 restricted licence banks and 29 deposit-taking companies in Hong Kong. Altogether, 200 authorised institutions (excluding representative offices) from 31 countries and territories (including Hong Kong) had a presence in Hong Kong.
- (6) The figures for private sector debt may not represent a full coverage of all the Hong Kong dollar debt paper issued.
- (7) Assets of the banking sector include notes and coins, amount due from authorised institutions in Hong Kong as well as from banks abroad, loans and advances to customers, negotiable certificates of deposits (NCDs) held, negotiable debt instruments other than NCDs held, and other assets. Certificates of indebtedness issued by Exchange Fund and the counterpart bank notes issued are nevertheless excluded.

- (8) Moody's also upgraded the Mainland government's long-term foreign currency bond rating by one notch to "A1" simultaneously, while Standard & Poor's also revised the Mainland's rating outlook from "Stable" to "Positive."
- (9) The ranking is sourced from the World Federation of Exchanges, a global trade association for the stock exchange industry. Its membership comprises 55 securities exchanges (as of 25 January 2008), covering almost all globally recognised stock exchanges.
- (10) At end-2007, there were 1 048 and 193 companies listed on the Main Board and GEM respectively.
- (11) At end-2007, there were 47 classes of stock options contracts and 43 classes of stock futures contracts.
- (12) These figures are sourced from the Sales and Redemptions Survey conducted by the Hong Kong Investment Funds Association on their members, and cover only the active authorised funds that have responded to the survey. To provide a more accurate picture of the retail fund market in Hong Kong, the survey has been revamped, with effect from 2005, such that it would cover only retail transactions (including switching) and exclude institutional transactions. At end-2007, there were a total of 1 162 authorised-funds covered by the Survey.
- (13) There were 19 approved trustees at end-2007. On MPF products, 34 master trust schemes, two industry schemes and two employer sponsored schemes, comprising altogether 324 constituent funds, were approved by the Mandatory Provident Fund Schemes Authority. A total of 239 000 employers, 2.13 million employees and 271 000 self-employed persons have participated in MPF schemes.
- (14) There were 14 retail hedge funds authorised by the Securities and Futures Commission (SFC) and the net asset size of SFC-authorised hedge funds amounted to US\$1.73 billion as at end-2007, up by 4.2% from end-2006. The net asset size at end-2007 was more than 10 times of that as at end-2002, the year when the hedge funds guidelines were first issued.
- (15) As at end-2007, there were 178 authorised insurers in Hong Kong. Within this total, 47 were engaged in long-term insurance business, 112 in general insurance business, and 19 in composite insurance business. These authorised insurers come from 24 countries and territories (including Hong Kong).

CHAPTER 6 : THE LABOUR SECTOR

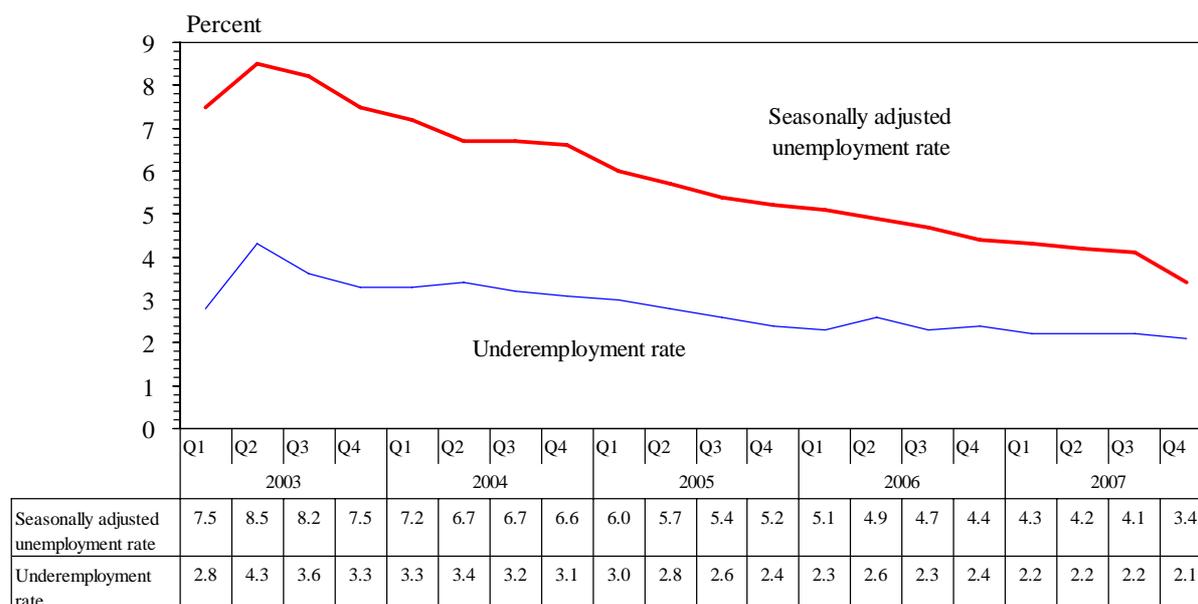
Summary

- *After three years of solid improvement, the labour market tightened visibly further in 2007, on the back of sustained economic expansion.*
- *Total employment showed an accelerated increase in 2007, reaching a historic high of over 3.53 million at year-end. Significant growth was particularly found in the domestically-oriented economic sectors and among lower-end workers.*
- *As employment growth continued to outstrip labour supply growth, unemployment eased noticeably further. The seasonally adjusted unemployment rate dropped to 3.4% in the fourth quarter of 2007, the lowest level for more than nine and a half years. The long-term unemployment rate also fell below 1% towards the year-end.*
- *Overall labour wages and earnings remained on the rise, though with considerable variation among different economic sectors and job categories.*

Overall labour market situation

6.1 The labour market continued to show encouraging performance in 2007. Benefiting from vibrant business activity and keen manpower requirement, total employment expanded at a rate which outpaced that in labour supply for the fourth year in a row, even though increasing number of people were prompted to enter the labour market by the brighter job prospects. This factor, along with the increasing shift in growth impetus towards domestic demand, led to a further decline in unemployment⁽¹⁾, especially among lower-skilled workers and in the domestically-oriented sectors. The underemployment⁽²⁾ situation also improved. Reflecting the increased tightness in the labour market, labour incomes increased further and posted larger gains in some economic sectors and occupations. Job vacancies in the corporate sector continued to surge, rising to a post-1997 high for the month of September. The solid expansion in labour demand is spreading to more economic sectors and more occupations.

Diagram 6.1 : Backed by the sustained economic upturn, unemployment situation continued to improve in 2007, especially towards the year-end



Total employment and labour supply

6.2 In 2007, employers further stepped up recruitment in response to continued robust economic growth. *Total employment*⁽³⁾ kept rising and reached a record high of 3 533 300 in the fourth quarter, up by 2.0% over a year earlier. For the year as a whole, employment grew at an average of 2.5%, faster than the 2.1% rise in 2006. While the import/export trades and business services sectors remained major sources of job creation, other domestically-oriented sectors such as repair, laundry, domestic and miscellaneous personal services; restaurants; amusement and recreational services; as well as construction (especially decoration and maintenance) also registered solid job gains. Contrary to the development during 2006, in which employment growth occurred primarily at the upper segment, more job opportunities were also available to lower-skilled workers over the course of 2007, in particular service workers and shop sales workers and those engaged in elementary occupations. Younger workers aged 15-19 and older ones aged 50 or above, as well as persons with lower secondary and matriculation education were also among the chief beneficiaries of the employment growth in 2007.

6.3 *Labour supply*⁽⁴⁾ also expanded at a faster pace in 2007. In the fourth quarter, the labour force was estimated at 3 651 100, up by 1.0% over a year earlier. More notable growth, at 1.7%, was recorded for the year as a whole, representing a pick-up from 1.2% in 2006. The labour supply growth in 2007 was mainly attributable to the increased participation of older persons aged 50

or above, in particular females, probably due to better employment outlook and more job opportunities. For 2007 as a whole, the labour force participation rate for females averaged at 53.2%, up from 52.6% in 2006, while that for males declined from 70.9% to 70.6%.

6.4 Comparing end-2007 with the trough in mid-2003, total employment climbed up by 366 300 or 11.6%, more than doubled the increase of 177 300 or 5.1% in the labour force over the same period. In spite of a much stronger demand for higher-skilled workers during the earlier phase of the economic recovery, demand for lower-skilled workers also began to gather momentum more recently, as the economic upturn had become more entrenched and as domestic demand had played a greater role in driving economic growth. For instance, out of the 84 800 jobs created in 2007, about three-quarters were found in the lower segment. Seen in this light, the domestically-oriented sectors had not only become our major growth impetus, but also principal drivers of job creation.

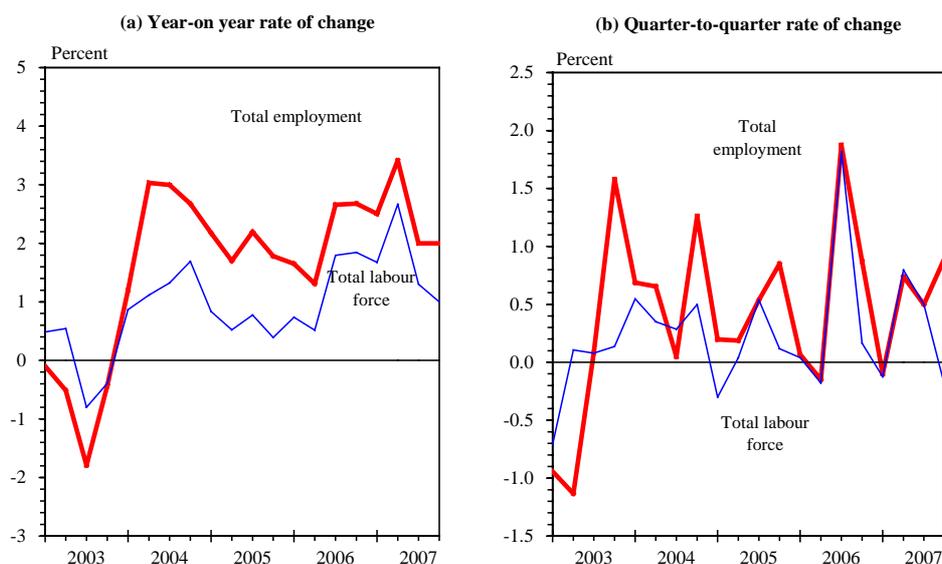
Table 6.1 : The labour force, and persons employed, unemployed and underemployed

		<u>Labour force</u>	<u>Persons employed</u>	<u>Persons unemployed^(a)</u>	<u>Persons underemployed</u>
2006	Annual	3 581 400 (1.2)	3 410 200 (2.1)	171 200	86 200
	Q1	3 552 400 (0.7)	3 374 900 (1.7)	177 500	80 100
	Q2	3 546 100 (0.5)	3 369 900 (1.3)	176 200	93 000
	Q3	3 610 600 (1.8)	3 433 100 (2.7)	177 500	84 000
	Q4	3 616 500 (1.8)	3 462 900 (2.7)	153 600	87 500
2007	Annual	3 640 500 (1.7)	3 495 000 (2.5)	145 600	79 400
	Q1	3 611 900 (1.7)	3 459 400 (2.5)	152 500	80 600
	Q2	3 640 700 (2.7)	3 485 000 (3.4)	155 700	81 200
	Q3	3 658 400 (1.3)	3 502 200 (2.0)	156 300	80 500
	Q4	3 651 100 (1.0)	3 533 300 (2.0)	117 800	75 500
		<-0.2>	<0.9>		

Notes : (a) These include first-time job-seekers and re-entrants into the labour force.
 () Year-on-year % change.
 <> % change between Q3 and Q4 (i.e. October-December).

Source : General Household Survey, Census and Statistics Department.

Diagram 6.2 : Both total employment and labour force showed accelerated increases in 2007, with growth in the former still outpacing the latter throughout the year

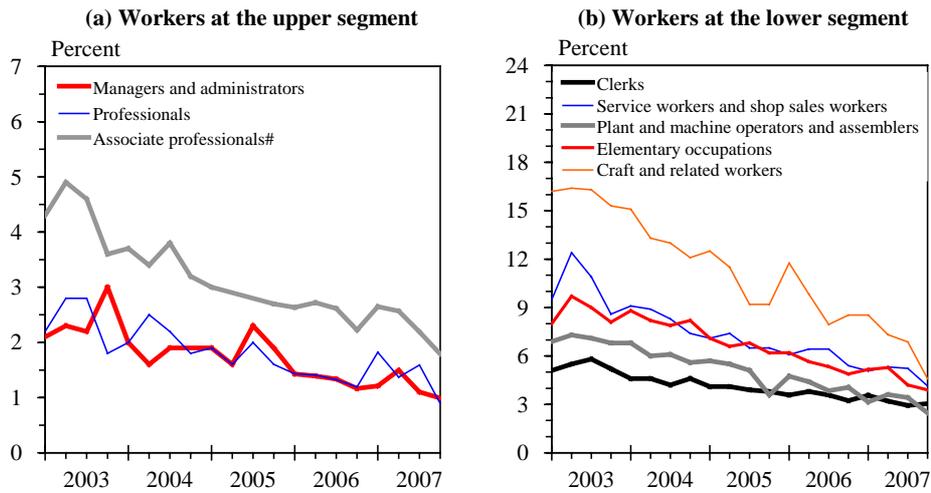


Profile of unemployment

6.5 Following the downward trend starting from mid-2003, unemployment continued to fall over the course of 2007. In the latter part of the year, the numbers unemployed dropped visibly, to 117 800 in the fourth quarter, below the 120 000 mark for the first time since February – April 1998. The seasonally adjusted unemployment rate, having edged down gradually during the first three quarters, fell at a much faster pace to 3.4% in the fourth quarter, the lowest level since January – March 1998. As in the past few years, lower-skilled workers experienced a greater reduction in unemployment rate, from 5.5% in 2006 to 4.5% in 2007, as against the fall from 2.0% to 1.8% for higher-skilled workers. Yet contrary to earlier years, the decline in unemployment among lower-skilled workers in 2007 was mainly demand-driven, indicating that these workers were able to enjoy increased job opportunities and share the fruits of sustained economic growth. The improvement was especially impressive for craft and related workers; service workers and shop sales workers and individuals engaged in elementary occupations.

6.6 In terms of demographic attributes, declines in unemployment rate were observed across virtually all age-sex groups, with the greatest reductions among young male workers aged 15-24 and older male workers aged 50-59. In the former case, the fall in unemployment was characterised by larger shrinkage in labour supply than in employment, particularly so among those aged 20-24. In the latter case, the improvement was brought about by faster employment growth relative to labour supply growth.

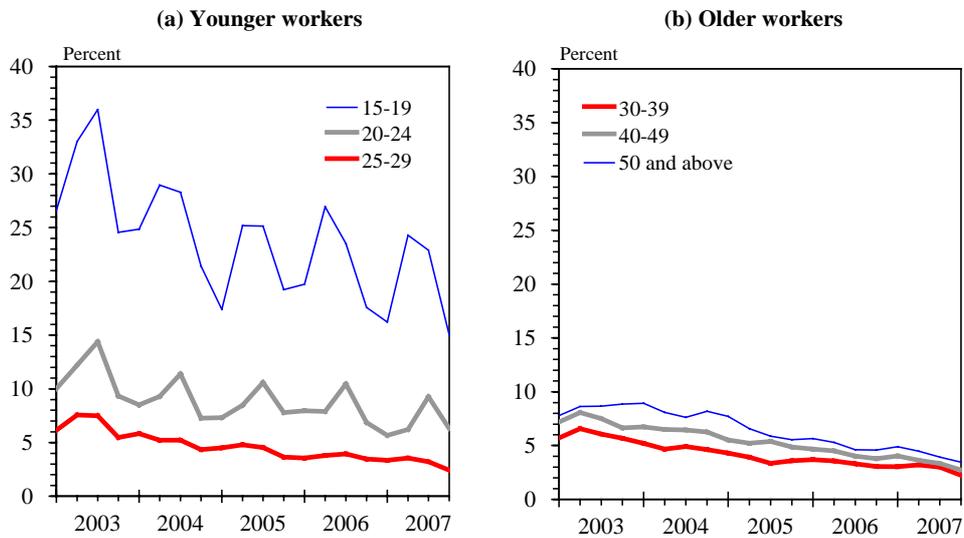
Diagram 6.3 : Lower-skilled workers were the chief beneficiaries of falling unemployment* in 2007



Notes : (*) Not seasonally adjusted, and not including first-time job seekers and re-entrants into the labour force.

(#) Including technicians and supervisors.

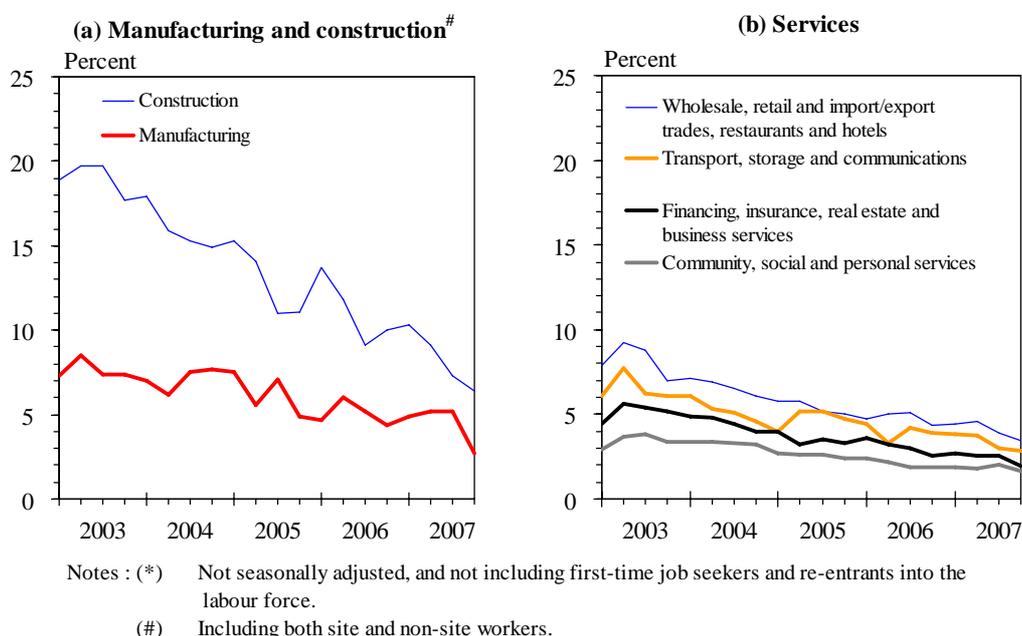
Diagram 6.4 : Workers of all ages saw declines in unemployment*



Note : (*) Not seasonally adjusted, but including first-time job seekers and re-entrants into the labour force.

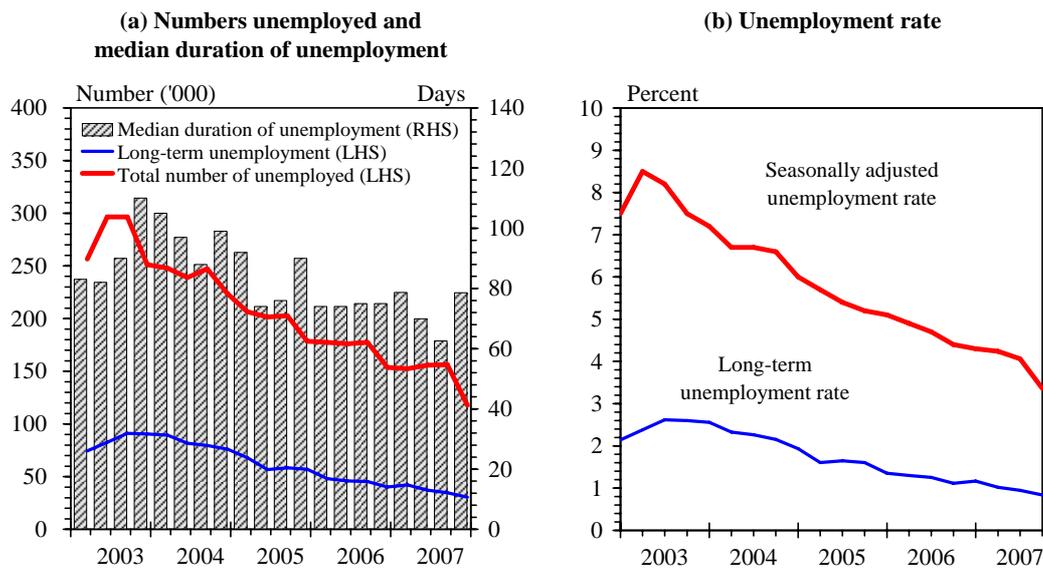
6.7 From a sectoral perspective, the improvement in unemployment situation was also widespread. More notable declines in unemployment rate were observed in the construction, restaurants, and real estate sectors. In particular, the unemployment rates for the construction and restaurants sectors fell substantially from 11.2% and 8.2% in 2006 to 8.3% and 6.1% in 2007 respectively. While the magnitudes in question were influenced by varying manpower resource conditions in these two sectors, both improvements were principally demand-driven. In contrast, the decline in unemployment rate in the real estate sector from 4.4% in 2006 to 2.7% in 2007 was mainly attributable to shrinkage in labour supply.

Diagram 6.5 : Unemployment rate* drifted lower across all major economic sectors in 2007



6.8 Indicators measuring the intensity of unemployment were similarly positive. For 2007 as a whole, the median duration of unemployment shortened slightly further from 74 days to 72 days. Meanwhile, with the number of long-term unemployed persons (i.e. unemployed for six months or longer) coming down to 30 600 in the fourth quarter, the long-term unemployment rate fell to 0.8%, the lowest level since mid-1998. Long-term unemployment fell most noticeably among persons engaged in the construction, transport, real estate and restaurants sectors, those engaged in lower-end jobs like craft and related workers and plant and machine operators and assemblers, as well as older workers with lower educational attainment. In this regard, greater employment growth for lower-skilled workers not only pushed down headline unemployment, but also eased the extent of skill mismatch in the local labour market.

Diagram 6.6 : Long-term unemployment* eased further



Profile of underemployment

6.9 For 2007 as a whole, the underemployment situation improved slightly. The total number of underemployed persons fell from 86 200 in 2006 to 79 400 in 2007, and the underemployment rate from 2.4% to 2.2%. This suggests that more and more employers were willing to hire permanent staff to cope with their business expansion, which in turn created more full-time jobs and helped ease underemployment. In parallel with the improvement in unemployment situation, workers in the lower segment, like craft and related workers, service workers and shop sales workers, as well as workers in elementary occupations enjoyed more notable declines in underemployment rate. Concurrently, greater declines in underemployment rate were observed in the decoration and maintenance construction, restaurants and sanitary services sectors. Mirroring these sectoral and occupational profiles, younger workers aged 15-24 and middle-aged female workers with lower secondary education or below benefited most from the falling underemployment in 2007.

Box 6.1

Seasonal adjustment of the unemployment rate

The unemployment rate compiled on a moving three-month basis and released every month by the Census and Statistics Department (C&SD) is seasonally adjusted. The main purpose of seasonal adjustment is to facilitate meaningful comparison of unemployment rate figures for different periods in a year and to enhance understanding and interpretation of the underlying trend.

At present, C&SD adopts the X11-ARIMA method, which is a widely-used seasonal adjustment method, to remove the effect of seasonal variations for the unemployment rate and related series. Under the X11-ARIMA model, the original series (O) is assumed to be the product of seasonal component (S), trend-cycle component (T) and irregular component (I) (i.e. $O_t = S_t \times T_t \times I_t$ at time t). The moving average approach is used to decompose these components and derive the seasonal factors. The seasonally adjusted series is then obtained by dividing the original series by the seasonal factors.

An indirect approach is adopted to compile the seasonally adjusted unemployment rate. First, seasonally adjusted numbers of employed persons and unemployed persons are separately derived by the X-11 ARIMA method. The seasonally adjusted unemployment rate is then measured as the proportion of seasonally adjusted unemployed persons in the seasonally adjusted labour force, the latter being the sum of the seasonally adjusted employed persons and the seasonally adjusted unemployed persons. The main reason for adopting the indirect approach is to ensure that all such seasonally adjusted figures are arithmetically consistent.

In practice, seasonal factors for a given year are first projected on the basis of past data. The length of the past data used for projections is not fixed and is determined by comparing the results using data of different lengths according to a set of statistical assessment criteria. This is to ensure that seasonal patterns of the early years that have become obsolete are no longer taken into account in the projection. For example, the seasonal factors for 2007 were projected in February 2007 based on the data for 2000-2006. These projected factors were used to calculate the seasonally adjusted numbers of employed persons and unemployed persons for different periods in 2007. The Table and Chart below show the seasonal factors so derived for 2007.

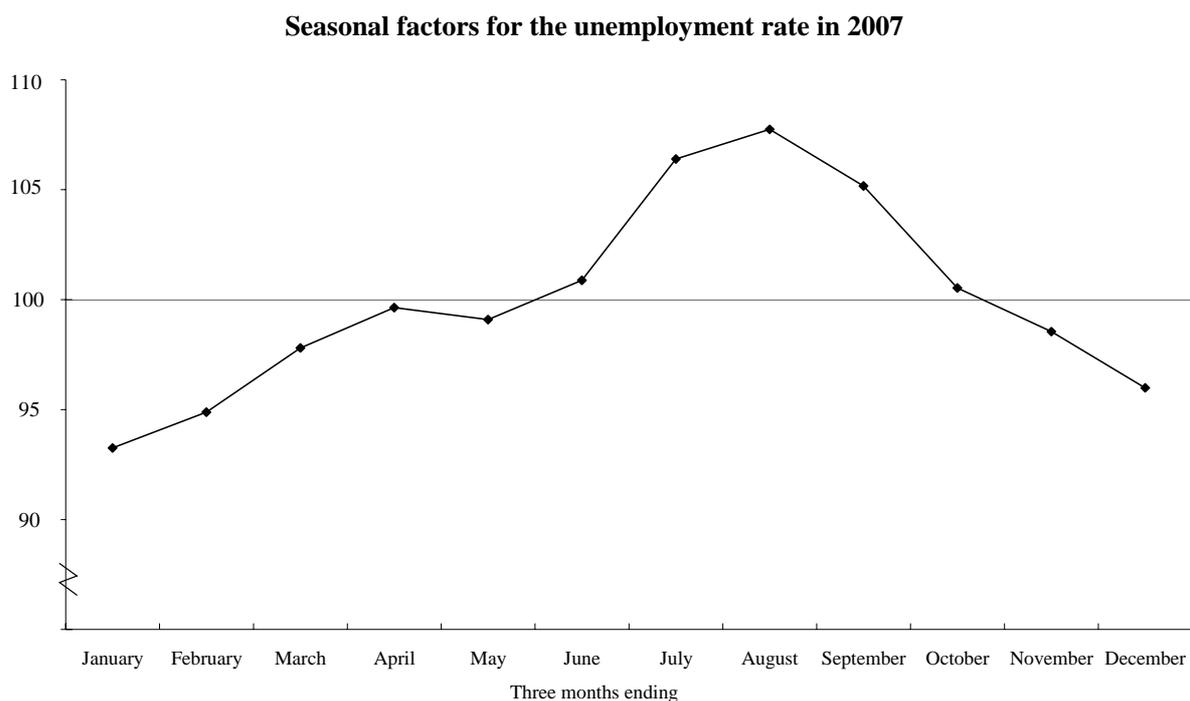
Seasonal factors⁽¹⁾ for the number of employed persons and unemployed persons and the unemployment rate in 2007

Three-month ending	Seasonal factors for the number of employed persons	Seasonal factors for the number of unemployed persons	Seasonal factors ⁽²⁾ for the unemployment rate
January	100.43	93.36	93.25
February	100.06	94.75	94.88
March	100.06	97.75	97.80
April	99.68	99.28	99.64
May	99.73	98.81	99.09
June	99.65	100.57	100.88
July	99.69	106.39	106.40
August	99.93	108.03	107.75
September	99.97	105.38	105.17
October	100.14	100.71	100.53
November	100.23	98.74	98.55
December	100.43	96.23	95.99

Notes: (1) The average seasonal factor for a year is 100. A seasonal factor above 100 means the number of employed/unemployed persons for that month is more than the average, whereas a seasonal factor below 100 means the number for that month is less than the average.

(2) Implicitly derived based on the ratio of the original unemployment rate (i.e. not seasonally adjusted) over the seasonally adjusted unemployment rate

Box 6.1 (Cont'd)



A number of salient observations follow from the seasonal factors in the above table/chart:

1. While the seasonal factors for the employment series are statistically significant, they range very narrowly between 99.6 and 100.5. The employment level is seasonally high around the Christmas and Lunar New Year holidays (with the highest seasonal factor in a year recorded in October-December or November-January) and seasonally low before the summer time (with the lowest seasonal factor in a year recorded in April-June).
2. The seasonal factors for the unemployment series have larger variations across different three-month periods, ranging from 93.4 to 108.0. Contrary to the employment series, the unemployment level is seasonally low around the Christmas and Lunar New Year holidays (with the lowest seasonal factor in a year recorded in November-January). This is mainly attributable to the strong labour demand at these festive times and the relatively low turnover of employees before the receipt of year-end double pay and bonuses. On the other hand, the unemployment level is seasonally high during the summer times (with the highest seasonal factor in a year recorded in June-August) when there are a large number of school leavers and graduates entering the labour market. Given the small variations of the seasonal factors for the employment series, the seasonal factors for the unemployment rate are very close to those for the unemployment level.

Box 6.2

An analysis of the One-High-Two-Low group⁽¹⁾

What is the One-High-Two-Low group?

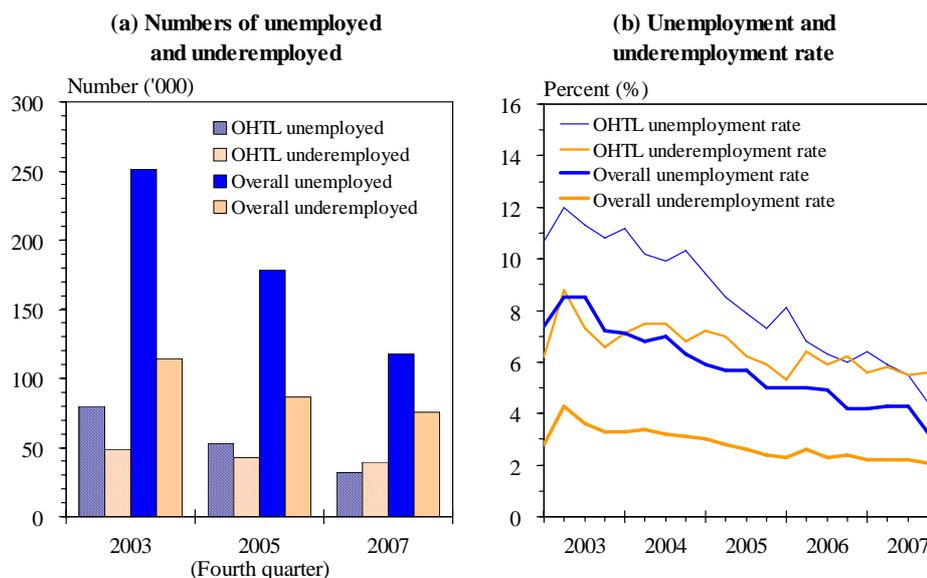
Strong and sustained economic expansion over the past few years has led to a broad-based improvement in the labour market conditions. Workers in virtually all segments have benefited, including those who belong to the One-High-Two-Low (OHTL) group. The OHTL group consists of workers aged 40 or over, with lower secondary education or below who are engaged in lower-skilled occupations. These workers are often perceived to be vulnerable and under-privileged as they tend to experience greater difficulties in finding and holding jobs, and hence to face greater risk of long-term unemployment. This note aims to provide a detailed analysis of this group, especially the question of whether the individuals concerned would be able to share the fruits of the current economic expansion.

Unemployment and underemployment situation of the OHTL group

In tandem with the robust job creation during the economic upswing, employment in the OHTL group rose from 659 300 in Q4 2003 to 687 400 in Q4 2007, an average of 1.0% per annum. This figure is significantly lower than the corresponding increase of 2.3% in total employment. Nevertheless, given the decrease in the OHTL labour force from 739 400 to 718 900 over the same period, the numbers unemployed in the OHTL group fell significantly from 80 100 to 31 500, and the unemployment rate from 10.8% to 4.4%. As a result, the unemployment gap between the OHTL group and the total labour force (including FDHs) narrowed considerably over the years. Employment gains in the OHTL group was particularly notable since late 2006, reflecting that even workers in the lower segment have also been able to enjoy more job opportunities as the economic recovery becomes full-fledged and entrenched.

Over the same period, underemployment in the OHTL group also improved, though by a lesser extent, with the number and rate declined respectively from 49 100 and 6.6% to 39 900 and 5.6%. However this favourable trend conceals the fact that the OHTL underemployment rate has remained persistently high and well above the economy-wide average in the past two years (5.6% vis-à-vis the overall average of 2.1% (including FDHs) in Q4 2007).

The OHTL group has also benefited from the economic upturn⁽²⁾



(1) Unless otherwise stated, this analysis excludes foreign domestic helpers (FDHs).

(2) The overall unemployment and underemployment figures here include FDHs.

Box 6.2 (cont'd)

OHTL labour force by age and sex

Compared to the overall labour force aged 40 or over (the One-High or OH group), the OHTL group comprises a greater proportion of older persons, i.e. those aged 50 or over, and also exhibits a more notable ageing trend in recent years. In Q4 2007, the size of OHTL labour force aged 50 or over was 409 600, up from 345 700 in Q4 2003 with increases observed in both sexes. The respective proportion of older persons in the OHTL labour force likewise rose from 46.8% to 57.0%, significantly faster than that observed in the OH labour force, from 38.7% to 44.0%.

The gender mix of the OHTL labour force has also changed. With a decline in male workers aged 40-49 which more than offset the increase in older males, the OHTL male labour force shrank by 7.3% from 460 200 to 426 600 between Q4 2003 and Q4 2007. In contrast, the OHTL female labour force increased by 4.7% from 279 200 to 292 400 over the same period, although a dip in the number of females aged 40-49 was also observed. As a result, the share of females in the total OHTL labour force rose from 37.8% to 40.7%. Analysed by major economic sector, notable declines in OHTL male labour force were found in the manufacturing, retail trade, and restaurant sectors. While a portion of these male workers may have exited the labour force for reasons such as retirement or discouragement over employment prospects, some of them have conceivably upgraded their skills through further study, training or retraining, thereby moving out of the OHTL group. In comparison, the increase in OHTL female labour force occurred mostly in such service sectors as sanitary and similar services, import and export trade, and business services.

Employment status of the OHTL group

Concomitantly with the expansion of OHTL female labour force, the number of employed OHTL females registered a larger increase of 23 000, as against 5 100 for their male counterparts between Q4 2003 and Q4 2007. Also noteworthy is the significant compositional change in the employment status of these females. While a notable decline in underemployed females was found, this was more than offset by the increases in those working on full-time and voluntary part-time basis. Many of the originally underemployed OHTL female workers may have been able to switch to full-time employment amid the economic upswing, while numerous part-time jobs have also been created for OHTL females who voluntarily choose to work shorter hours to supplement family income. In contrast, the composition of employment status of OHTL males was fairly stable over the same period. Specifically, the number of underemployed OHTL males remained high, which in turn contributed to the persistently high underemployment rate for the whole OHTL group. A significant portion (67%) of the underemployed OHTL males in Q4 2007 were engaged as craft and related workers or in elementary occupations in the construction sector.

Employed OHTL workers by sex and employment status*

	Male			Female		
	Q4 2003	Q4 2007	Change	Q4 2003	Q4 2007	Change
Full-time	355 000	356 300	+1 300	208 100	224 100	+16 100
Underemployed	30 700	31 100	+400	18 400	8 800	-9 600
Voluntary part-time	16 600	20 000	+3 400	30 600	47 000	+16 400
Total	402 300	407 400	+5 100	257 000	280 000	+23 000

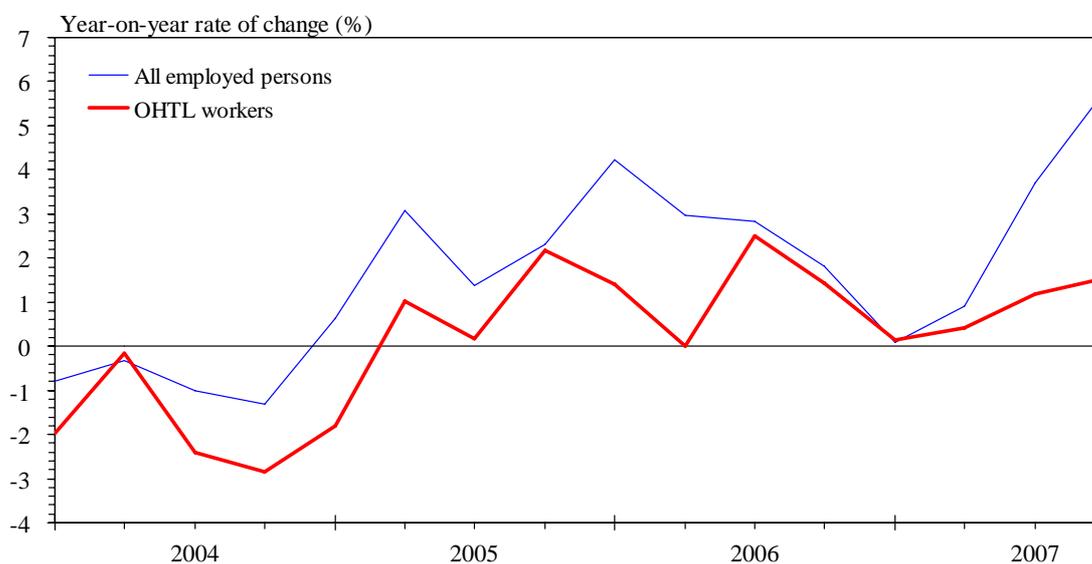
Note: (*) Full-time workers refer to those working 35 hours or longer during the 7 days before the enumeration, whilst voluntary part-timers are those working less than 35 hours but not underemployed (involuntarily working shorter hours).

Box 6.2 (cont'd)

Earnings trend of the OHTL group

Benefiting from the general uptrend in labour wages and particular the improving unemployment and underemployment situation among the OHTL group, OHTL workers have enjoyed earnings increase since mid-2005. In Q4 2007, average employment earnings of the OHTL group rose by 1.5% over a year earlier. Nevertheless, as depicted by the diagram below, earnings growth of OHTL workers has been persistently below the overall average. In addition to the higher proportion of underemployed and voluntary part-time workers in this group who tend to have lower earnings, the ongoing structural transformation towards a knowledge-based economy, which has led to greater demand for better educated and higher-skilled professional and managerial staff and hence a faster increase in their salaries, is also a contributing factor.

Average employment earnings of OHTL workers also on the rise, though at a relatively modest pace



Conclusion

The robust economic expansion and improvements in the labour market in the past few years have benefited workers from all walks of life, including the OHTL group. Given this outcome, it is believed that the most effective and fundamental way to improve the livelihood of lower end workers is to stimulate economic growth and create more employment opportunities. The relatively modest earnings growth of OHTL workers vis-à-vis the overall average points to the importance of investment in education, training, retraining and employment assistance measures to enhance the abilities of the disadvantaged, so as to better equip them to adapt to economic restructuring.

Profile of employment in establishments

6.10 Statistics on employment, vacancies and labour income in the private sector are only available up to the third quarter of 2007. Comparing September 2007 with a year earlier, employment in *private sector establishments* increased by 2.2%. Sustained strong economic growth, together with buoyant financial sector activity, fuelled impressive job gains in such higher value-added services as wealth management and financial advisory. Robust consumer spending and vibrant inbound tourism also helped to boost job creation in domestically-oriented activities. Employment growth was therefore particularly notable in the financing, insurance, real estate and business services; and restaurants and hotels sectors. As for the community, social and personal services sector, major job gains came from the sub-sectors like medical, dental, other health and veterinary services, largely underpinned by booming consumer-centric industries. On the other hand, owing to the slack in public infrastructure and the increased service-orientation of the local economy, employment at building and construction sites⁽⁵⁾ and the manufacturing sector declined further by 7.7% and 2.6% respectively. In terms of size of establishment, larger enterprises dominated in job creation. All in all, this group accounted for about two-thirds of the total job gains in September 2007, with the rest being accounted for by small and medium-sized enterprises (SMEs)⁽⁶⁾. Taking the first nine months of 2007 together, the number of persons engaged in private sector establishments increased by 2.3% over a year earlier.

6.11 As for the *civil service*, employment edged down slightly by 0.2% year-on-year in September 2007, following the 0.5% decline in June 2007. With the phasing-out of the general open recruitment freeze as from 1 April 2007 and the gradual step-up in recruitment for civil service posts, the prolonged downtrend of civil service employment can be expected to end presently.

Table 6.2 : Employment by major economic sector

	<u>2006</u>					<u>2007</u>		
	<u>Annual average</u>	<u>Mar</u>	<u>Jun</u>	<u>Sep</u>	<u>Dec</u>	<u>Mar</u>	<u>Jun</u>	<u>Sep</u>
Wholesale, import and export trades	583 400 (0.3)	581 200 (-0.3)	581 700 (0.4)	584 000 (-0.2)	586 600 (1.2)	587 500 (1.1)	588 200 (1.1)	586 500 (0.4)
Retail trade	228 300 (3.3)	225 900 (4.6)	229 300 (2.1)	228 600 (3.1)	229 400 (3.4)	229 100 (1.4)	232 600 (1.5)	233 100 (2.0)
Restaurants and hotels	226 400 (5.1)	221 800 (5.3)	225 800 (5.3)	226 200 (5.5)	231 800 (4.3)	231 700 (4.4)	232 500 (3.0)	237 300 (4.9)
Transport and storage	155 700 (1.6)	154 100 (1.8)	155 200 (1.0)	156 100 (1.8)	157 500 (1.9)	155 900 (1.2)	160 100 (3.1)	160 000 (2.5)
Communications	29 600 (-1.4)	30 000 (0.6)	29 300 (-5.9)	29 500 (-0.7)	29 400 (0.8)	30 300 (0.8)	30 100 (2.7)	29 800 (1.1)
Financing, insurance, real estate and business services	479 100 (5.0)	468 300 (4.6)	475 900 (4.1)	480 500 (5.5)	491 600 (5.8)	492 000 (5.1)	503 200 (5.7)	509 300 (6.0)
Community, social and personal services	454 800 (3.6)	451 300 (3.9)	451 700 (3.4)	455 200 (4.0)	460 800 (3.1)	464 200 (2.9)	467 900 (3.6)	465 400 (2.2)
Manufacturing	160 500 (-2.5)	161 500 (-1.0)	161 100 (-0.5)	160 200 (-3.7)	159 300 (-4.8)	158 700 (-1.7)	157 300 (-2.3)	156 000 (-2.6)
Building and construction sites	52 900 (-10.8)	54 900 (-16.5)	52 300 (-12.9)	53 300 (-6.3)	51 000 (-6.3)	50 400 (-8.3)	51 100 (-2.2)	49 200 (-7.7)
<i>All establishments surveyed in the private sector^(a)</i>	2 378 700 (2.1)	2 357 200 (2.0)	2 370 400 (1.8)	2 381 800 (2.3)	2 405 300 (2.4)	2 407 800 (2.1)	2 430 900 (2.6)	2 434 500 (2.2)
		<0.7>	<0.3>	<0.6>	<0.8>	<0.4>	<0.7>	<0.3>
<i>Civil service^(b)</i>	154 300 (-1.3)	155 000 (-1.5)	154 500 (-1.5)	154 100 (-1.4)	153 800 (-1.1)	153 800 (-0.8)	153 700 (-0.5)	153 800 (-0.2)

Notes : Employment figures enumerated from business establishments, as obtained from the Quarterly Survey of Employment and Vacancies, are somewhat different from those enumerated from households, as obtained from the General Household Survey. This is mainly due to difference in sectoral coverage: while the former survey covers selected major sectors, the latter survey covers all sectors in the economy.

(a) The total figures on private sector employment cover also employment in mining and quarrying and in electricity and gas supply, besides employment in the major sectors indicated above.

(b) These figures cover only those employed on civil service terms of appointment. Judges, judicial officers, ICAC officers, locally engaged staff working in Hong Kong Economic and Trade Offices abroad, and other Government employees such as non-civil service contract staff are not included.

() % change over a year earlier.

< > Seasonally adjusted quarter-to-quarter % change.

Sources : Quarterly Survey of Employment and Vacancies, Census and Statistics Department.
Quarterly Employment Survey of Construction Sites, Census and Statistics Department.

Vacancies

6.12 In September 2007, vacancies in *private sector establishments* reached 52 300, up significantly by nearly 20% over a year earlier to the highest level for the month of September since 1997. Almost all of these vacancies emerged in the services sector, with the most distinct growth in restaurants and hotels; community, social and personal services; and financing, insurance, real estate and business services sectors. Similar growth rates in vacancies were recorded at both the higher and lower ends (19.8% vs. 20.0%), indicating that the economic upturn had fed through to benefit even workers in the lower segment. When unemployment statistics were introduced, further analysis gave a ratio of 33 job vacancies per 100 job-seekers in September 2007, up from 25 a year earlier and extending the uptrend beginning since the latter part of 2003. The corresponding ratio for higher-skilled jobs jumped from 71 to 95, whereas that for lower-skilled jobs went up from 21 to 30. In terms of size of establishment, large enterprises and SMEs recorded similar vacancy growth in September 2007 of 20.8% and 19.1% respectively. With regard to the *civil service*, a total number of 3 000 vacancies and a 6.0% year-on-year increase were observed in September 2007.

6.13 Statistics supplied by the Employment Services of the Labour Department provide indication of the latest changes in job vacancies. In the fourth quarter of 2007, the number of private sector job vacancies leaped by 41.0% over a year earlier to 153 401. For 2007 as a whole, the increase remained appreciable, at 16.6% to 559 815. On average, more than 2 200 vacancies were received per working day. At the same time, the department achieved a total of 135 489 placements in 2007, up by 13.9%. The 2007 figures were all-time highs.

6.14 In addition to regular employment services, the Labour Department has periodically arranged general or theme-specific job fairs at different locations. In 2007, 10 large-scale and 114 district-based job fairs were organised to facilitate job matching especially at the lower end of the labour market. The larger-scale job fairs were well attended by over 187 prospective employers, offering some 15 500 vacancies. As a new initiative to further promote youth employment, the Labour Department set up the first Youth Employment Resource Centre called “Youth Employment Start” (Y.E.S.) in Langham Place, Mongkok in December 2007. The centre provides one-stop advisory and support services on employment and self-employment to youngsters aged between 15 and 29. The Department is now making preparation for the second Y.E.S. in Kwai Fong.

Diagram 6.7 : Vacancies surged across almost all occupations and reached a post-1997 high for the month of September

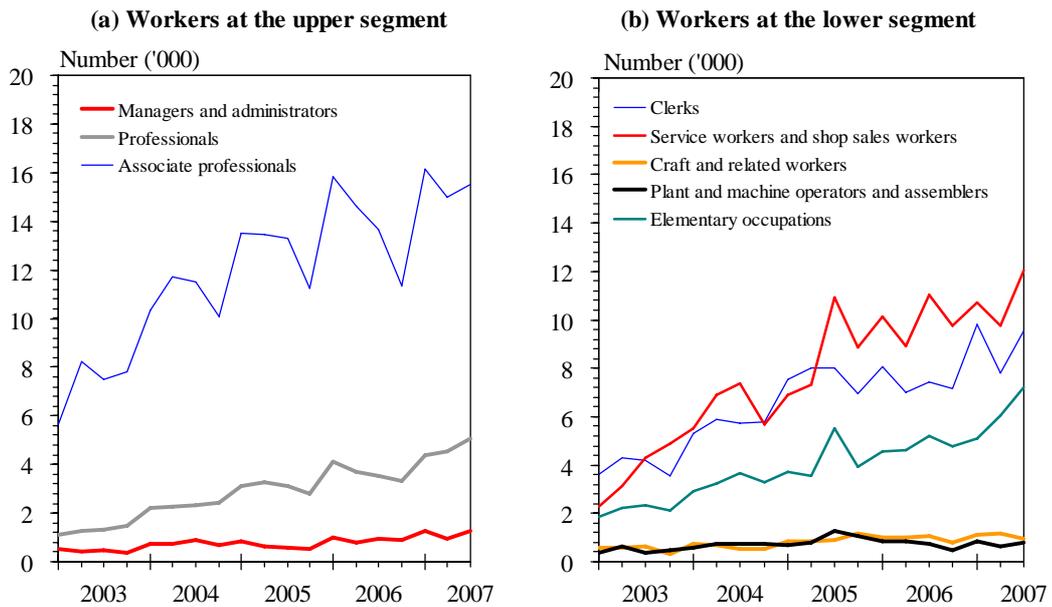
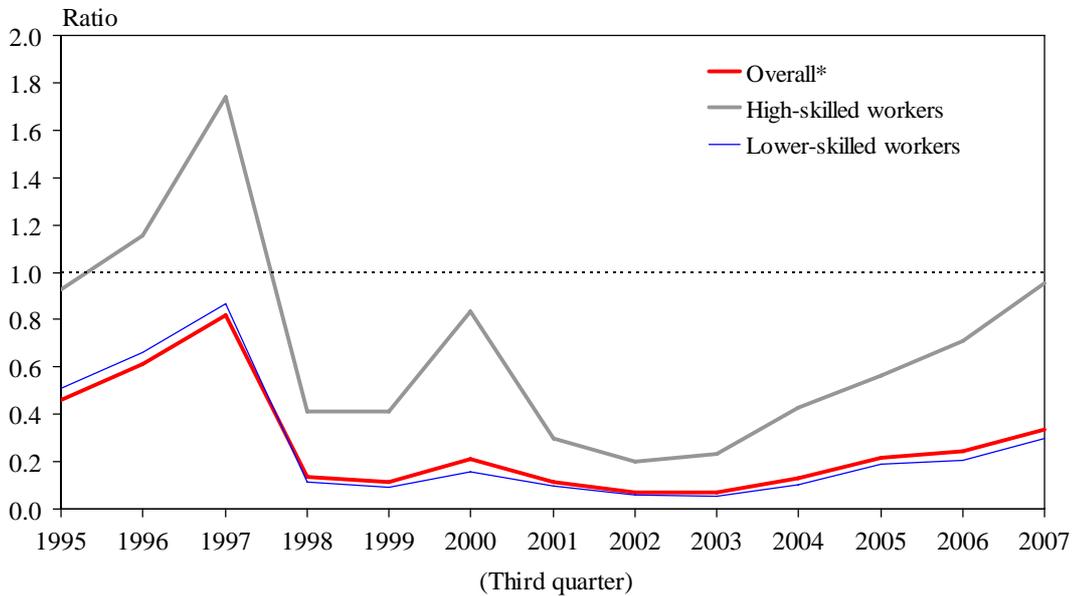


Diagram 6.8: Vacancy-to-applicant ratio went up since the third quarter of 2003



Note : (*) Including first-time job seekers and re-entrants into the labour force.

Table 6.3 : Vacancies by major economic sector

	<u>No. of vacancies</u>									
	<u>Annual average</u>	<u>2006</u>				<u>2007</u>				<u>Vacancy rate in Sep 2007 (%)</u>
		<u>Mar</u>	<u>Jun</u>	<u>Sep</u>	<u>Dec</u>	<u>Mar</u>	<u>Jun</u>	<u>Sep</u>		
Wholesale, import and export trades	8 400 (-8.2)	10 600 (3.0)	8 300 (-10.8)	7 800 (-14.2)	6 800 (-12.9)	10 400 (-1.8)	9 000 (8.6)	8 800 (13.5)	1.5	
Retail trade	4 300 (16.2)	4 800 (58.7)	3 800 (17.4)	4 400 (-9.1)	4 200 (13.2)	5 100 (5.5)	4 200 (10.3)	5 100 (17.3)	2.2	
Restaurants and hotels	4 200 (22.6)	4 000 (63.4)	4 000 (45.3)	5 000 (17.6)	3 700 (-11.3)	4 300 (6.8)	4 500 (12.7)	6 600 (31.5)	2.7	
Transport and storage	2 000 (6.5)	2 000 (20.1)	2 200 (17.5)	1 800 (-19.6)	1 700 (17.5)	2 200 (7.1)	2 200 (-0.4)	2 300 (26.3)	1.4	
Communications	700 (0.8)	800 (93.0)	800 (52.6)	700 (-42.6)	700 (-15.4)	800 (3.0)	800 (-3.8)	1 000 (51.9)	3.3	
Financing, insurance, real estate and business services	12 300 (13.2)	13 600 (29.6)	12 300 (9.6)	12 800 (6.8)	10 500 (7.6)	14 600 (7.7)	13 700 (11.8)	14 800 (16.2)	2.8	
Community, social and personal services	8 600 (20.7)	7 900 (15.6)	8 100 (13.3)	9 200 (15.1)	9 300 (40.6)	9 600 (22.3)	9 500 (16.6)	11 400 (23.6)	2.4	
Manufacturing	1 900 (-6.4)	1 900 (-3.4)	2 000 (6.1)	1 900 (-3.7)	1 700 (-22.5)	2 400 (23.3)	2 000 (-1.6)	2 100 (11.7)	1.3	
Building and construction sites	# (-7.0)	# (66.7)	# (*)	# (*)	# (-23.8)	# (660.0)	# (77.8)	# (160.0)	0.1	
All establishments surveyed in the private sector ^(a)	42 300 (9.1)	45 500 (22.8)	41 500 (9.3)	43 600 (0.1)	38 600 (5.7)	49 300 (8.3)	45 900 (10.5)	52 300 (19.9)	2.1	
		<2.2>	<-3.5>	<0.7>	<6.7>	<4.2>	<-0.8>	<8.2>		
Civil service ^(b)	2 500 (166.7)	2 600 (76.3)	2 500 (131.6)	2 900 (308.8)	2 100 (304.0)	1 200 (-55.0)	3 200 (27.0)	3 000 (6.0)	1.9	

Notes : Vacancy rate refers to the ratio of vacancies to total employment opportunities (actual employment plus vacancies).

(a) The total figures on private sector vacancies cover also vacancies in mining and quarrying and in electricity and gas supply, besides vacancies in the major sectors indicated above.

(b) These figures cover only vacancies for those staff to be employed on civil service terms of appointment. A general open recruitment freeze to the civil service was imposed during the period from 1 April 2003 to 31 March 2007. The civil service vacancies during this period refer only to the number of vacant posts for which exemptions from open recruitment freeze have been granted.

() % change over a year earlier.

< > Seasonally adjusted quarter-to-quarter % change.

(#) Less than 50.

(*) Less than 0.05%.

Sources : Quarterly Survey of Employment and Vacancies, Census and Statistics Department.
Quarterly Employment Survey of Construction Sites, Census and Statistics Department.

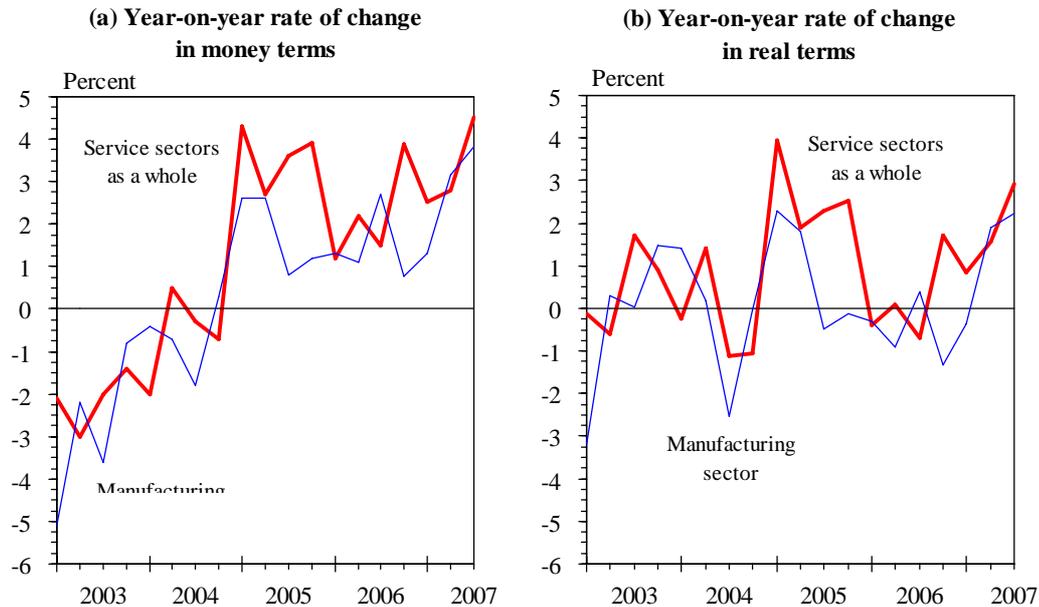
Earnings and wages

6.15 Employment income has been rising steadily since early 2005, though with varying magnitude across different economic sectors. In the third quarter of 2007, *labour earnings*⁽⁷⁾, as measured by payroll per person engaged in the private sector, increased by 4.6% in money terms over a year earlier. After adjusting for inflation, labour earnings went up by 3.0% in real terms⁽⁸⁾. Taking the first three quarters of 2007 together, labour earnings rose by 3.3% in money terms and 1.8% in real terms over a year earlier.

6.16 In the third quarter of 2007, nominal pay rises were observed in nearly all economic sectors. Yet, mainly due to the different labour demand and supply situations, the exact magnitude displayed considerable variation across economic sectors. As in the preceding few quarters, workers in financial institutions continued to enjoy larger gains in nominal payroll of 6.7% from a year earlier. By comparison, labour earnings in other service sectors like transport, storage and communications, wholesale and retail trades, restaurant and hotels posted more moderate, although still solid, increases of 3 - 4%. As for the community, social and personal services sector, the pick-up in pay rise to 4.6% was mainly boosted by some one-off factors like the back-pay for workers in the education services and medical services sectors. Therefore, such notable pay increase should not be interpreted as completely reflective of fundamental manpower resource conditions.

6.17 More up-to-date data from the General Household Survey indicated that the overall average monthly employment earnings (excluding foreign domestic helpers) registered an accelerated year-on-year increase of 5.8% in money terms in the fourth quarter of 2007, mainly driven by larger pay hikes in the upper segment. Anecdotal evidence generally suggests that as the labour market has become increasingly tight with rising staff turnover, more and more enterprises have had to offer more attractive remuneration packages in order to maintain service levels and retain staff.

Diagram 6.9 : Nominal earnings posted a faster increase in the third quarter of 2007, partly boosted by the salary back-pay in the education and medical services sectors



6.18 Compared with labour earnings, *labour wages*, as a measure of regular payments to employees at the supervisory level or below, showed a smaller year-on-year increase of 2.3% in money terms in September 2007. The rate of increase was the same for the first nine months of 2007 as a whole. After netting out the price change, wages edged up by 1.3% in real terms in September 2007 and 1.0% for the first nine months as a whole.

6.19 More detailed statistics revealed that both nominal and real wages for all major economic sectors and job categories went up. Similar to the case of labour earnings, the increases varied in accordance with demand and supply situation in the different segments. Benefiting from the positive sentiment in the consumer and financial markets, workers in the personal services; and financing, insurance, real estate and business services sectors had the greatest nominal wage increases of 6.5% and 3.0% respectively. Simultaneously, nominal wages for workers in transport services also edged up by 2.0%. Among workers in different occupational hierarchy, supervisory and technical workers enjoyed the largest increases in nominal wages, by 2.8%. Concurrently, average wages received by miscellaneous non-production workers; and clerical and secretarial workers also rose by 2.3% and 2.1% respectively. Judging from the above figures, it is not difficult to conclude that Hong Kong's economic upturn had not only generated significant pay rises for higher-skilled workers, but also brought pay increases to more and more workers at the lower-end.

Notes :

- (1) For a person aged 15 or above to be classified as unemployed, he or she should: (a) not have a job and not be performing any work for pay or profit during the reference period (i.e. seven days before enumeration); and (b) be available for work during the reference period; and (c) be seeking work during the 30 days before enumeration.

Notwithstanding the above, the following types of persons are also considered unemployed: (a) persons without a job, having sought work but not available for work because of temporary sickness; (b) persons without a job, available for work but not having sought work because they will take up new jobs or start business at a subsequent date, or expect to return to their original jobs; and (c) discouraged workers not having sought work because they believe work is not available to them.

Even at full employment, some frictional unemployment is bound to exist as workers move between jobs in order to obtain better terms of employment. The precise level of unemployment which can be described as purely frictional varies amongst economies, depending on the structure and characteristics of their labour markets.

In April 2001, the Census and Statistics Department put out a revised series of seasonally adjusted unemployment rate compiled by reference to the X-11 ARIMA method, which adjusts for all seasonal variations in employment and unemployment (i.e. the changes due to holiday effects, seasonally ups and downs in economic activity, seasonal variations in first-time job-seekers, etc). This replaces the former series which adjusts only for seasonal variations in the proportion of first-time job-seekers in the labour force. For more details, see Note (3) at the end of Chapter 5 of the Half-yearly Economic Report 2001 and also Box 6.1 of this Chapter.

Figures enumerated from the General Household Survey have been revised to take into account the results of the 2006 Population By-census. Labour force figures compiled for the period from Q1 2001 to Q4 2006 have also been revised.

The revision has the effect of lowering the levels of total labour force, total employment, and the unemployed and underemployed by a modest margin. The effect on the unemployment and underemployment rates, being computed as ratios of the respective levels, is generally even smaller. Furthermore, the movements in the seasonally adjusted unemployment rate and the underemployment rate mostly showed little change.

- (2) The main criteria for an employed person aged 15 or above to be classified as underemployed are: involuntarily working less than 35 hours during the reference period (i.e. seven days before enumeration), and either available for additional work during the reference period or seeking additional work during the 30 days before enumeration.

Following these criteria, employed persons taking no-pay leave due to slack work during the reference period are also classified as underemployed if they had worked less than 35 hours or were on leave for the entire reference period.

- (3) Figures enumerated from household data. The employed population is defined here to include those persons aged 15 or above who performed work for pay or profit or had a formal job attachment during the reference period (i.e. seven days before enumeration).

- (4) The labour force, or the economically active population, is defined to include all persons aged 15 or above who either were engaged in productive work during the reference period (i.e. seven days before enumeration) or would otherwise have been engaged in productive work but were unemployed.
- (5) Taking into account off-site workers and related professional and support staff, employment in the entire building and construction sector actually increased by 3.2% in 2007 over 2006.

Employment for the construction sector as a whole is enumerated from the General Household Survey carried out by the Census and Statistics Department. Apart from site workers, it also includes non-site workers engaged in minor alteration and addition, repair, maintenance and interior decoration work on existing buildings. In addition, it includes professionals, administrative and other support personnel engaged in that sector, such as engineers, architects, surveyors and contract managers, as well as general clerical staff.

- (6) Manufacturing enterprises with fewer than 100 employees and non-manufacturing enterprises with fewer than 50 employees are regarded as small and medium-sized enterprises (SMEs) in Hong Kong. Yet, establishments with the same main business registration number (BRN) and engaging in activities of the same industry sector are grouped into one business unit for the purpose of calculating the number of SMEs. Thus, a business with a lot of small chain stores each employing a small number of employees will be considered as a single large enterprise, instead of separate SMEs.
- (7) In addition to wages, which include all regular payments like basic pay and stipulated bonuses and allowances, earnings also cover overtime pay and other non-guaranteed or irregular bonuses and allowances, except severance pay and long service payment. Because of this difference, as well as the difference in sectoral and occupational coverage, the movements in average earnings, as measured by payroll per person engaged, do not necessarily match closely with those in wage rates.
- (8) Different consumer price indices are used for compiling the real indices of labour earnings and wages, taking into account their relevance to the respective occupation coverage. Specifically, the Composite CPI, being an indicator of overall consumer prices, is taken as the price deflator for earnings received by employees at all levels of the occupational hierarchy. The CPI(A), being an indicator of consumer prices for the middle to lower income groups, is taken as the price deflator for wages in respect of workers on occupations up to the supervisory level, and also in respect of manual workers engaged in the construction sector.

CHAPTER 7 : PRICES

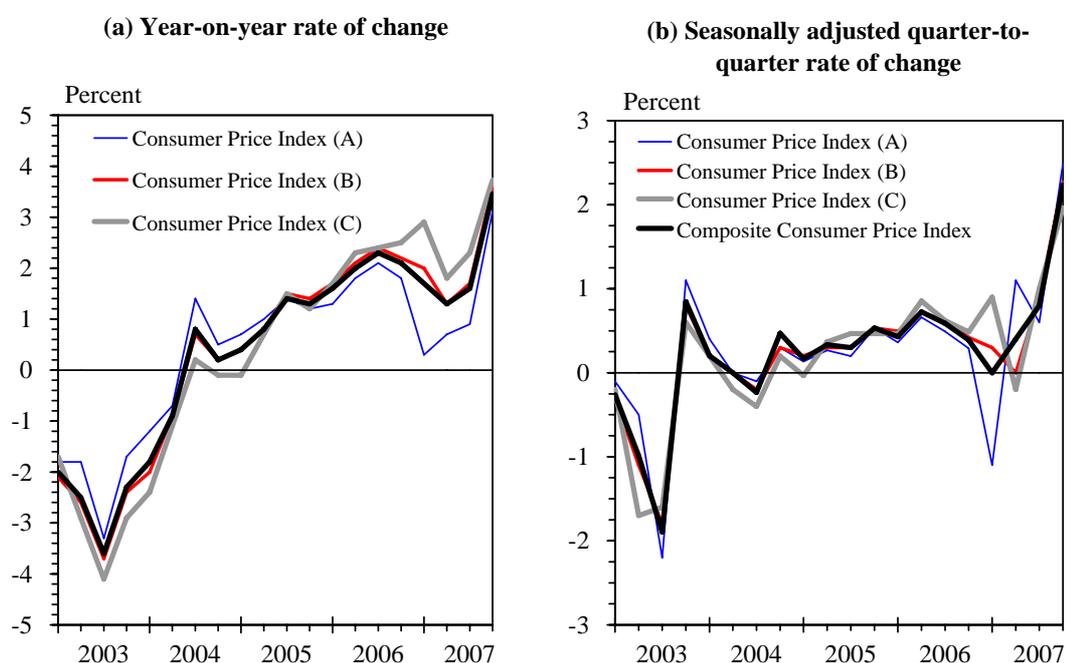
Summary

- *Consumer price inflation in 2007 averaged at 2.0% in terms of the Composite CPI, the same as in 2006. Discounting the effects of the public housing rental waiver in February and the rates concession in the second and third quarters of the year, the underlying consumer price inflation for 2007 as a whole was 2.8%, which was still rather moderate when viewed against the strong economic upturn over the past few years.*
- *Inflation pressures picked up in the second half of 2007, mainly due to higher food prices brought about by the global food inflation. The strong domestic demand, appreciation of the renminbi, weakening of the US dollar, and resurgence of international oil prices also contributed.*
- *Local business cost pressures were still largely contained in 2007. Unit labour cost continued to be kept down by rapid productivity growth, while unit rental cost remained in check, despite rising shop rentals, thanks to the rapid expansion in business volume.*
- *Looking ahead, the high food and oil prices, renminbi appreciation and weakening of the Hong Kong dollar will continue to exert pressures on prices from the external front. On the domestic front, rising private housing rentals may pose an upside risk to inflation. Also, the vibrant business activities and tightening labour market will likely further push up wages, and office and shop rentals. Yet the sustained labour productivity growth should provide some cushioning effect. Also, the measures announced in the 2007-08 Policy Address and the 2008-09 Budget will help lower the cost of living of the community and push down somewhat the headline inflation.*

Consumer prices

7.1 Continuing the upward trend in 2005 and 2006, the underlying inflation pressures continued to climb up over the course of 2007, reflecting the robust domestic demand as well as stronger external cost pressures. While the headline consumer price inflation for 2007 as a whole, as indicated by the *Composite Consumer Price Index (CCPI)*⁽¹⁾, at 2.0%, was the same as that for 2006, the former number was lowered by the public housing rental waiver in February 2007 and the rates concession in the second and third quarters of the year. Taking away the effects of these measures, the underlying consumer price inflation for 2007 was 2.8%, which was still rather moderate taking into consideration the robust economic growth for four consecutive years. Local business cost pressures were kept largely in check in 2007. Wages rose moderately during the year, and the impact on business costs was much alleviated by rising labour productivity. Likewise, the impact from the rise in commercial rentals was to a large extent diluted by rapid expansion in business volume.

Diagram 7.1 : Consumer price inflation climbing up in 2007



7.2 The underlying consumer price inflation climbed up from 2.5% and 2.4% in the first and second quarters respectively to 2.7% in the third quarter, and notably further to 3.5% in the last quarter. The pick-up of the inflation rate in the second half of 2007, amidst strong consumption demand, was mainly caused by surging food prices stemming from the global food inflation, appreciation of the renminbi and weakening of the US dollar. The resurgence

of international oil prices from September 2007 and higher housing costs also contributed. In 2008, inflationary pressures are expected to persist, as the high food and oil prices, renminbi appreciation and weakening of the Hong Kong dollar will continue to exert pressures on prices from the external front. On the domestic front, the upward trend of private housing rentals deserves close monitoring. Also, due to the vibrant business activities and tightening labour market, there will likely be some further build-up of pressures on wages and commercial rentals. Yet the sustained labour productivity growth should mitigate the rising price pressures to some extent.

Diagram 7.2 : Inflation pressures climbed up during 2007, with more distinct increases in food prices

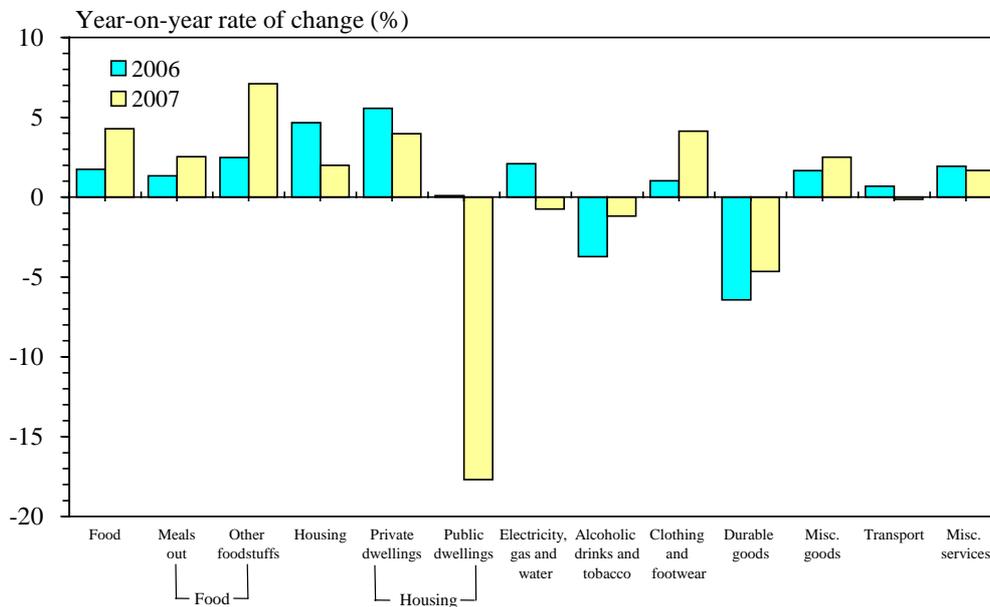


Table 7.1 : Consumer Price Indices
(year-on-year rate of change (%))

		<u>Composite CPI</u>	<u>CPI(A)</u>	<u>CPI(B)</u>	<u>CPI(C)</u>
2006	Annual	2.0	1.7	2.1	2.2
	H1	1.8	1.6	1.9	2.0
	H2	2.2	1.9	2.3	2.4
	Q1	1.6	1.3	1.7	1.7
	Q2	2.0	1.8	2.1	2.3
	Q3	2.3	2.1	2.4	2.4
	Q4	2.1	1.8	2.2	2.5
2007	Annual	2.0	1.3	2.2	2.7
	H1	1.5	0.5	1.7	2.3
	H2	2.5	2.0	2.7	3.0
	Q1	1.7	0.3	2.0	2.9
	Q2	1.3	0.7	1.3	1.8
	Q3	1.6	0.9	1.7	2.3
	Q4	3.5	3.1	3.6	3.7

**Table 7.2 : Composite Consumer Price Index by component
(year-on-year rate of change (%))**

<u>Expenditure component</u>	<u>Weighting (%)</u>	<u>2006</u>	<u>2007</u>	<u>2007</u>			
				<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>
Food	26.94	1.7	4.3	2.9	2.8	4.8	6.7
<i>Meals bought away from home</i>	<i>16.86</i>	<i>1.3</i>	<i>2.5</i>	<i>1.8</i>	<i>2.0</i>	<i>2.6</i>	<i>3.7</i>
<i>Other foodstuffs</i>	<i>10.08</i>	<i>2.5</i>	<i>7.1</i>	<i>4.4</i>	<i>4.1</i>	<i>8.2</i>	<i>11.6</i>
Housing ^(a)	29.17	4.7	2.0	2.2	1.0	0.7	4.2
<i>Private dwellings</i>	<i>23.93</i>	<i>5.6</i>	<i>4.0</i>	<i>5.6</i>	<i>2.0</i>	<i>2.3</i>	<i>5.9</i>
<i>Public dwellings</i>	<i>2.49</i>	<i>0.1</i>	<i>-17.7</i>	<i>-31.7</i>	<i>-10.5</i>	<i>-17.8</i>	<i>-10.8</i>
Electricity, gas and water	3.59	2.1	-0.7	-1.3	-2.2	-2.7	3.4
Alcoholic drinks and tobacco	0.87	-3.7	-1.2	-3.9	-0.1	-1.1	0.5
Clothing and footwear	3.91	1.0	4.1	7.2	3.9	3.7	2.0
Durable goods	5.50	-6.4	-4.7	-5.8	-4.6	-4.2	-4.0
Miscellaneous goods	4.78	1.7	2.5	2.8	1.8	2.1	3.4
Transport	9.09	0.7	-0.1	-0.6	-0.5	-0.1	0.7
Miscellaneous services	16.15	1.9	1.7	2.2	2.2	1.3	1.0
All items	100.00	2.0	2.0	1.7	1.3	1.6	3.5
			(2.8)	(2.5)	(2.4)	(2.7)	(3.5)

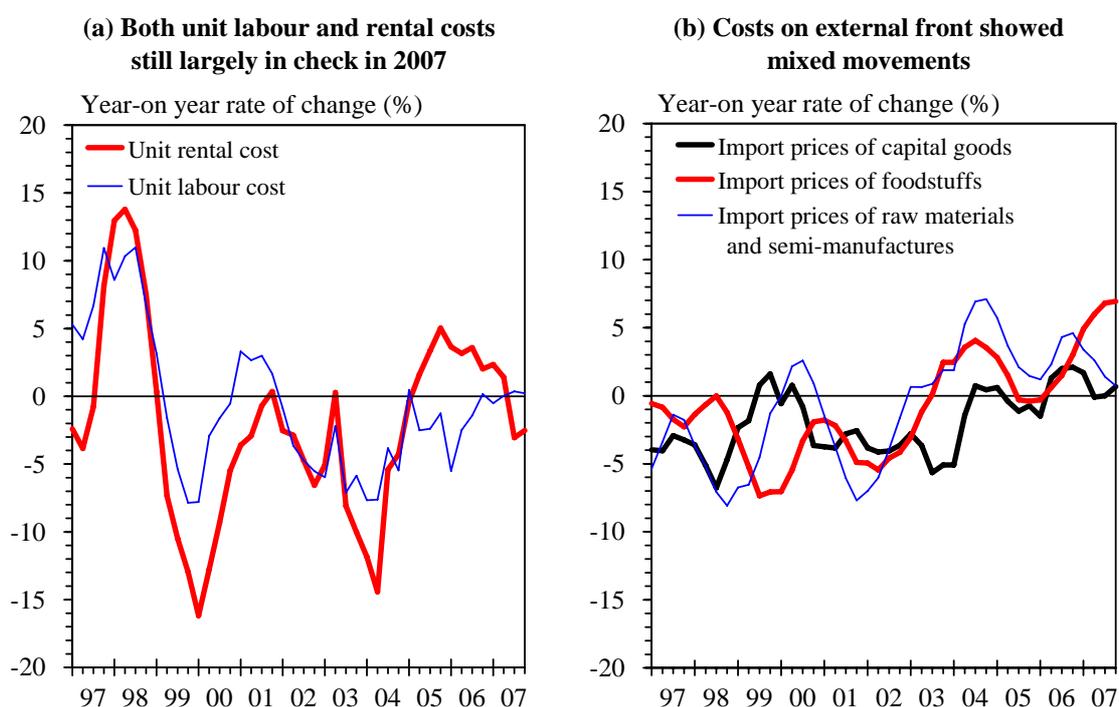
Notes : (a) The housing component covers rents, rates, Government rent, maintenance costs and other housing charges. Its sub-components on private and public dwellings as presented here, however, cover rents, rates and Government rent only. Hence, the combined weighting of private and public dwellings is slightly less than the weighting of the entire housing component.

() Underlying inflation rate after taking out the effects of the public rental waiver in February and the rates concession in the second and third quarters of 2007.

Costs of factor inputs

7.3 Along with the strong economic upturn, there have been increasing pressures on wages and rentals. However, the *unit labour cost*⁽²⁾ was still rather stable in 2007, thanks to the offset to higher wage costs by the sustained growth in labour productivity. As to *rental costs*, all business-related rentals on new leases, those for office space in particular, rose notably in 2007. Yet, on a per unit rental cost basis, the rise was so far contained due to rapid business expansion.

Diagram 7.3 : Costs of factor inputs



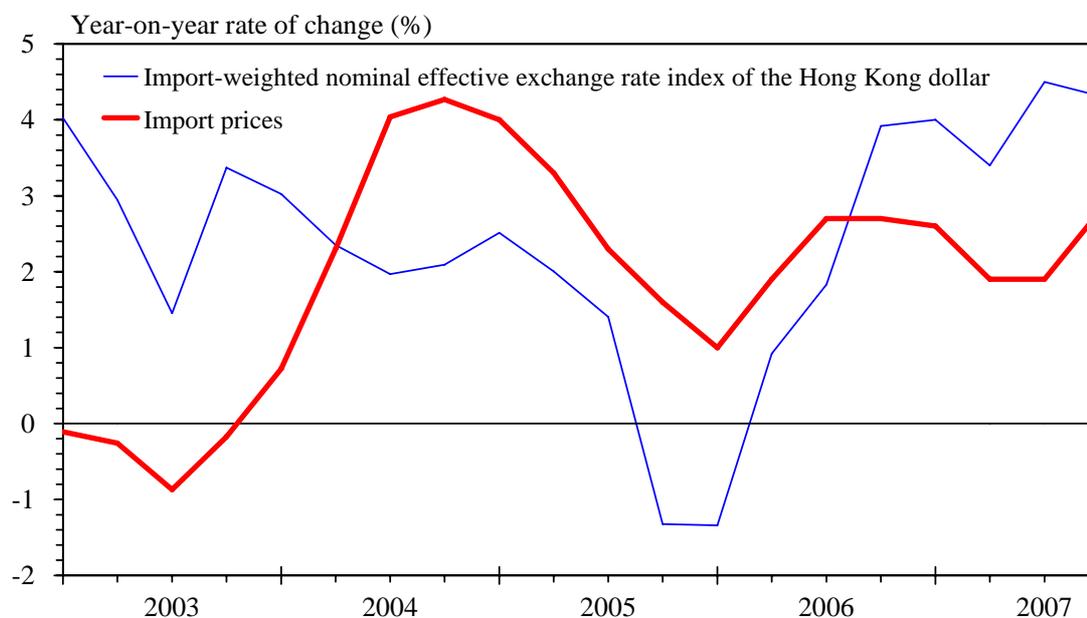
7.4 Despite the weakening of the Hong Kong dollar, the increase in import prices in overall terms remained moderate in 2007. Yet prices of different end-use categories showed very divergent movements. The import prices of *foodstuffs* went up notably over the course of the year due to inflation in food prices in the Mainland and other major source countries including Australia, Thailand and the US. Import prices of *fuels* shot up in the second half of the year along with the resurgence in international crude oil prices. The pick-up in prices of *consumer goods* was relatively milder thanks to the still moderate increases in prices of consumer goods from major sources including the Mainland and Japan. While these import prices which are more relevant to consumer price inflation saw faster increases, import prices of *raw materials* rose only modestly and those of *capital goods* were rather stable.

**Table 7.3 : Prices of imports by end-use category
(year-on-year rate of change (%))**

		<u>Foodstuffs</u>	<u>Consumer goods</u>	<u>Raw materials</u>	<u>Fuels</u>	<u>Capital goods</u>	<u>All</u>
2006	Annual	1.2	0.5	3.2	16.6	1.1	2.1
	H1	0.2	0.3	1.8	27.5	*	1.5
	H2	2.3	0.7	4.4	7.6	2.1	2.7
	Q1	-0.3	0.5	1.2	32.4	-1.5	1.0
	Q2	0.6	0.1	2.3	23.7	1.3	1.9
	Q3	1.5	0.4	4.3	13.6	2.0	2.7
	Q4	3.0	1.1	4.6	2.0	2.1	2.7
2007	Annual	6.2	3.3	2.0	11.2	0.5	2.3
	H1	5.4	2.8	3.0	0.3	0.7	2.2
	H2	6.9	3.7	1.1	22.2	0.3	2.3
	Q1	4.9	2.3	3.4	1.9	1.7	2.6
	Q2	6.0	3.2	2.6	-2.0	-0.1	1.9
	Q3	6.8	3.4	1.4	7.9	*	1.9
	Q4	6.9	4.0	0.7	37.1	0.7	2.8

Note : (*) Change of less than 0.5%.

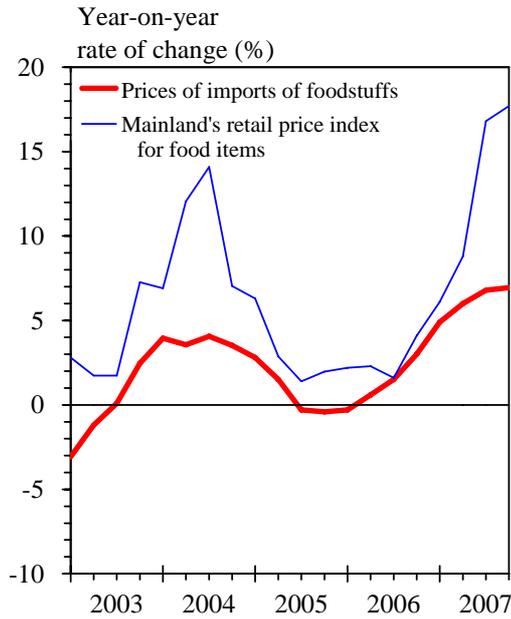
Diagram 7.4 : Import prices rose moderately further along with the weakening of the Hong Kong dollar



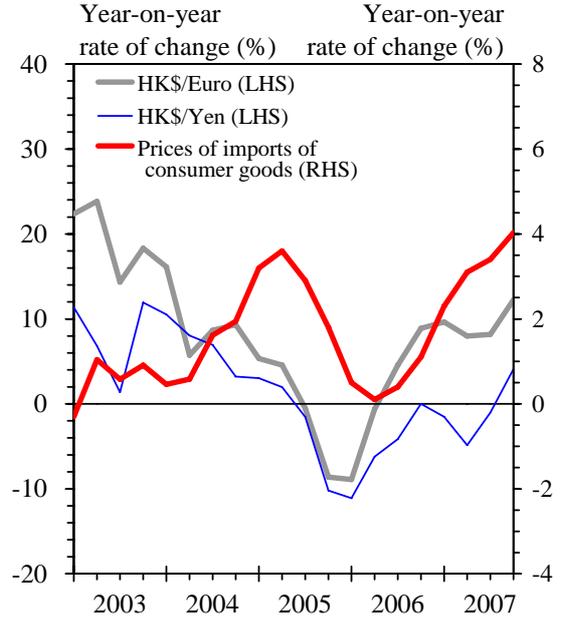
Note: The nominal EERI in this graph is inverted in scale for easier comprehension. An increase in the nominal EERI indicates weakening of the Hong Kong dollar.

Diagram 7.5 : Prices of imports by end-use category

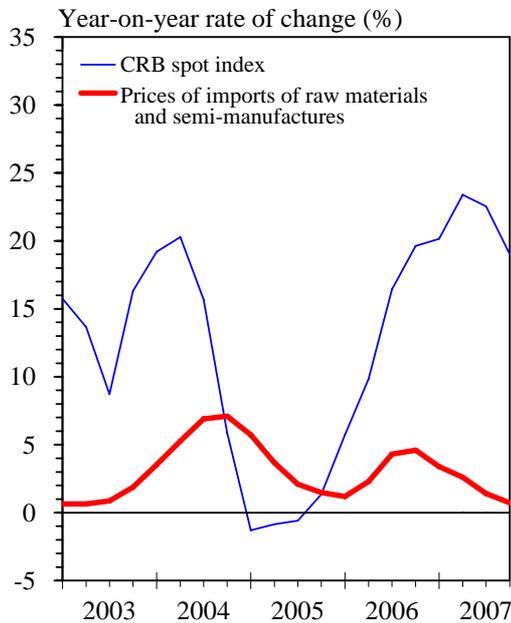
(a) Import prices of foodstuffs rose distinctly



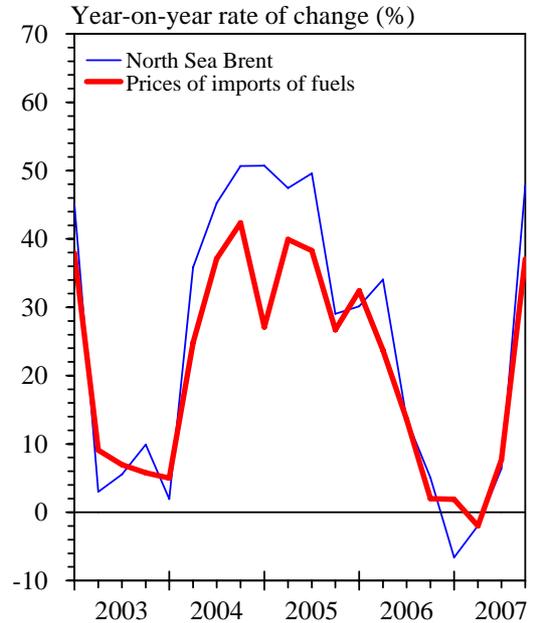
(b) Import prices of consumer goods picked up moderately



(c) Import prices of raw materials saw mild increases



(d) Fuel prices shot up in the second half of 2007



Output prices

7.5 Output prices of the local manufacturing sector, as measured by the *Producer Price Index*⁽³⁾, picked up modestly in the first three quarters of 2007. For the service sectors, output prices generally remained in check or even declined, reflecting the competitive business environment and the sustained growth in productivity. The only exception was the hotel sector, which saw a further sharp rise in prices, in tandem with the vibrant performance of inbound tourism during the year. The persistent decline in the output prices for the telecommunications sector reflected the keen competition and continued technological advancement in the sector. More recently, output prices of land transport and marine transport tended to rise amidst elevated fuel costs.

Table 7.4 : Producer Price Indices for the local manufacturing sector and selected service sectors (year-on-year rate of change (%))

<u>Industry group</u>	<u>Annual</u>	<u>Q1</u>	<u>2006</u> <u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>2007</u> <u>Q2</u>	<u>Q3</u> [@]
Manufacturing	2.3	2.0	2.4	2.6	2.0	2.5	2.6	2.5
Selected services sector ^(#)								
Hotels and boarding houses	10.3	10.1	9.2	9.2	12.5	8.4	9.2	10.1
Land transport	*	1.0	0.6	-0.2	-1.2	-0.8	-0.4	0.2
Maritime transport	-1.9	-3.6	-3.4	-1.8	1.1	1.8	-0.8	0.7
Air transport	-1.1	0.2	-0.5	-1.1	-3.0	0.8	1.4	-0.5
Telecommunications	-6.1	-7.5	-6.3	-4.0	-6.7	-3.4	-3.8	-2.6
Miscellaneous communications services	0.4	1.5	1.4	1.3	-2.6	-0.3	-0.7	-0.4

Notes : (#) Producer Price Indices for the other service sectors are not available, due to the difficulties involved in defining and delineating the various types of services and hence in measuring their respective price changes. This is particularly so for such sectors as banking and insurance, where the producers often do not charge their customers explicitly.

(*) Change of less than 0.05%.

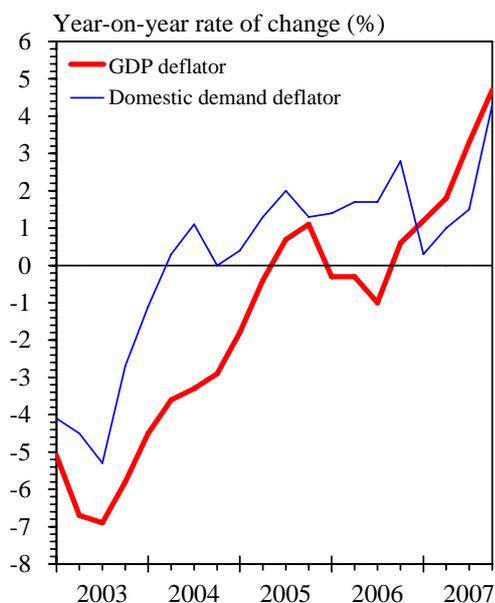
(@) Provisional figures.

GDP deflator

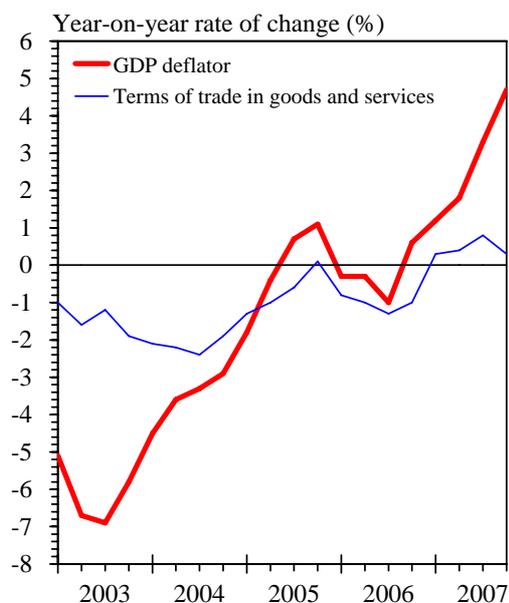
7.6 After declining marginally in 2006, the *GDP deflator*⁽⁴⁾, a broad measure of overall changes in prices of the economy, rose moderately in 2007, by 2.8% over a year earlier. This was mainly because the *terms of trade*⁽⁵⁾, which has a prominent impact on the GDP deflator given the sheer size of trade in the Hong Kong economy, improved during the year as export prices rose slightly faster than import prices. Taking out the trade components, the *domestic demand deflator* picked up by 1.9% on average in 2007. The increase was faster in the second half of the year, in line with the rising trend of consumer prices.

Diagram 7.6 : GDP deflator

(a) GDP deflator rose faster than domestic demand deflator in 2007



(b) ...reflecting the continued improvement in terms of trade



**Table 7.5 : GDP deflator and the main expenditure component deflators
(year-on-year rate of change (%))**

	<u>2006</u>					<u>2007</u>				
	<u>Annual[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Annual⁺</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4⁺</u>
Private consumption expenditure	1.3	1.5	1.4	0.7	1.6	3.8	1.9	2.3	3.9	6.6
Government consumption expenditure	1.2	1.0	1.4	1.3	1.2	3.3	1.3	4.0	3.9	4.0
Gross domestic fixed capital formation	4.2	1.3	3.6	6.0	5.8	-4.3	-4.3	-4.9	-6.7	-1.5
Total exports of goods	0.3	-1.2	0.1	0.6	1.2	2.1	2.3	1.7	1.7	2.5
Imports of goods	2.1	0.6	2.1	2.7	2.8	1.6	2.1	1.2	0.9	2.3
Exports of services	3.6	3.6	4.0	3.6	3.3	2.7	2.9	2.2	2.6	3.1
Imports of services	0.8	-0.3	0.4	1.1	1.7	2.9	2.3	2.5	2.9	3.7
Gross Domestic Product	-0.3	-0.3	-0.3	-1.0	0.6	2.8	1.2	1.8	3.3	4.7
		(-0.3)	(0.1)	(*)	(0.7)		(0.5)	(0.9)	(1.3)	(1.9)
Total final demand	1.2	0.2	1.1	1.3	2.0	2.1	1.8	1.5	1.8	3.2
Domestic demand	1.9	1.4	1.7	1.7	2.8	1.9	0.3	1.0	1.5	4.3

Notes : Figures are subject to revision later on as more data become available.

Figures in brackets are the seasonally adjusted quarter-to-quarter rates of change.

(#) Revised figures.

(+) Preliminary figures.

(*) Change of less than 0.05%.

Notes :

- (1) The Consumer Price Indices (A), (B) and (C) are compiled by reference to the average expenditure patterns for different groups of households as obtained from the Household Expenditure Survey. Then, by aggregating the expenditure patterns of all the households covered by the above three indices, a Composite CPI is compiled.

The expenditure ranges of the households covered in the 2004/05-based CPIs are shown below:

	<u>Approximate proportion of households covered</u> (%)	<u>Average monthly expenditure range during Oct 2004 to Sep 2005</u> (\$)
CPI(A)	50	4,000 to 15,499
CPI(B)	30	15,500 to 27,499
CPI(C)	10	27,500 to 59,999

The weightings of the various components in the 2004/05-based CPIs are as follows:

<u>Expenditure Component</u>	<u>Composite CPI (%)</u>	<u>CPI(A) (%)</u>	<u>CPI(B) (%)</u>	<u>CPI(C) (%)</u>
Food	26.94	32.10	27.32	20.41
<i>Meals bought away from home</i>	16.86	18.63	17.65	13.74
<i>Other foodstuffs</i>	10.08	13.47	9.67	6.67
Housing	29.17	30.54	27.70	29.66
<i>Private dwellings</i>	23.93	22.07	23.89	26.11
<i>Public dwellings</i>	2.49	6.18	1.25	--
<i>Maintenance costs and other housing charges</i>	2.75	2.29	2.56	3.55
Electricity, gas and water	3.59	4.84	3.37	2.45
Alcoholic drinks and tobacco	0.87	1.35	0.79	0.42
Clothing and footwear	3.91	2.81	4.28	4.67
Durable goods	5.50	4.01	5.67	6.99
Miscellaneous goods	4.78	4.68	4.76	4.91
Transport	9.09	8.07	9.05	10.35
Miscellaneous services	16.15	11.60	17.06	20.14
All items	100.00	100.00	100.00	100.00

- (2) Unit labour cost represents the labour cost per unit of output produced. It is distinct from the nominal wage index in that it will discount the effect of labour productivity growth in arriving at the labour cost measure. Technically, it refers to the product of the nominal index of payroll per person engaged and the total employment, divided by the real GDP.
- (3) The Producer Price Index is designed to reflect changes in the prices of goods and services received by local producers. Producer prices refer to the transacted prices, net of any discounts or rebates allowed to the buyers. Transportation and other incidental charges are not included.
- (4) The implicit price deflators of GDP and its main expenditure components are derived by dividing GDP at current prices by the corresponding volume estimates. The rate of change in the GDP deflator may differ substantially from that in the Composite CPI over the same time span. The Composite CPI covers consumer price inflation in particular. Yet the GDP deflator is a much broader measure of inflation for the entire economy, and takes into account all the price changes related to consumption, investment, exports and imports. Also, the rate of change in the GDP deflator may differ appreciably from that in the total final demand deflator, depending on the movements in the prices of final demand and imports. Likewise, the rate of change in the GDP deflator may differ appreciably from that in the domestic demand deflator, depending on the movements in the prices of imports and exports.
- (5) The terms of trade is defined as the ratio of the prices of total exports to the prices of total imports.

Calendar of Events of Significance for the Hong Kong Economy in 2007

1 Jan The liberalisation measures under the Supplement III to the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) came into effect. Hong Kong service suppliers enjoyed preferential access to the Mainland market in 27 service areas, which included 15 new liberalisation measures in 10 service areas. Moreover, the number of products with CEPA rules of origin agreed was increased to 1 448.

The Individual Visit Scheme (IVS), launched in 2003 to allow Mainland visitors to visit Hong Kong in their personal capacity, was extended to cover five more Mainland cities, namely, Shijiazhuang, Zhengzhou, Changchun, Hefei and Wuhan, bringing the total number of IVS cities to 49.

The Mainland continued to reduce its import tariffs on 44 items in line with her World Trade Organization (WTO) commitments. The average import tariff rate was 9.9% in 2007.

2 Jan The Government introduced a multiple entry permit system for river trade vessels to reduce the permit cost for these vessels by up to 50%. It was one of the measures to enhance Hong Kong Port's competitiveness.

9 Jan The first meeting of the Hong Kong-Zhuhai-Macao Bridge (HZMB) Task Force established by the Central Government was held in Guangzhou to help press ahead the HZMB project. The Task Force was chaired by the Vice Chairman of the National Development and Reform Commission, and consisted of representatives from the Ministry of Communications, Hong Kong and Macao Affairs Office and the three governments of Guangdong, Hong Kong and Macao as members.

The International Monetary Fund (IMF) released its Staff Report on Hong Kong. It was highly supportive of the Government's policy framework in fostering economic growth and maintaining the competitiveness of Hong Kong as an international financial centre. The IMF reiterated its support for the authorities' commitment to the Linked Exchange Rate system and noted that the Government was making commendable efforts to coordinate with the Mainland authorities on the use of Hong Kong's advanced financial infrastructure to improve the Mainland's financial intermediation, thereby benefiting both economies.

10 Jan The State Council agreed to a further expansion of renminbi business in Hong Kong, whereby Mainland financial institutions, upon obtaining approval, could issue renminbi-denominated bonds in Hong Kong.

15 Jan The Focus Group of Financial Services formed under the Economic Summit on "China's 11th Five-Year Plan and the Development of Hong Kong" released its Action Agenda, which included 80 recommendations covering securities, foreign exchange, commodities futures, insurance, reinsurance and asset management in pursuit of developing Hong Kong as China's international financial centre of global significance.

The People's Bank of China (PBOC) raised the renminbi reserve requirement ratio by 0.5 percentage point.

- 16 Jan The Heritage Foundation and the Wall Street Journal released the 2007 Index of Economic Freedom. Hong Kong was rated the freest economy in the world for the 13th straight year, followed by Singapore and Australia.
- 19 – 21 Jan The Chief Executive (CE) led a delegation of government officials and business leaders to visit Jiangxi.
- 24 Jan The Office of the Government Chief Information Officer (OGCIO) organised the symposium “Innovative Use of ICT – Enabling the Next Generation of Public Services”. The symposium aimed to facilitate government bureaux/departments, the academia and the information and communication technology (ICT) industry to exchange views on and explore opportunities for adoption of ICT in business operations of bureaux/departments.
- 5 Feb The Immigration Department (ImmD) started to issue new Hong Kong Special Administrative Region (HKSAR) Electronic passport (e-Passport). With the back cover embedding a contactless integrated circuit chip containing digital data pursuant to the standards specified by the International Civil Aviation Organization, and more than 40 anti-forgery features, the e-Passport had further safeguarded and promoted the travel convenience enjoyed by HKSAR passport holders. As of end-2007, more than 450 000 e-Passports were issued by ImmD.
- 8 Feb The Office of the Commissioner of Insurance (OCI) and the Isle of Man Insurance and Pensions Authority concluded a memorandum of understanding (MOU) to strengthen supervisory cooperation and exchange of information between the two regulators.
- 9 Feb The OCI and the Australian Prudential Regulation Authority concluded an MOU to strengthen supervisory cooperation and exchange of information between the two regulators.
- 14 Feb The “Be the Smart Regulator” Programme was launched to further enhance the business environment and competitiveness of Hong Kong and to improve the efficiency, transparency and business-friendliness of Hong Kong’s licensing system with the aim of reducing compliance costs to the business sectors. The Efficiency Unit and the Economic Analysis and Business Facilitation Unit had been coordinating with 29 bureaux/departments providing licensing services to various business sectors in taking forward a number of short- to long-term measures for continuous improvement of the licensing system.
- 16 Feb The Government received four tenders for the design and build contract of the Tamar Development Project upon the close of a 20-week tender invitation period.
- 25 Feb The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.
- 28 Feb The United Kingdom (UK) Foreign and Commonwealth Office presented to UK parliament the 20th Six-monthly Report on Hong Kong covering the period July to December 2006. The Report stated that the “One Country, Two Systems” principle had generally worked well in practice and that the rights and freedoms promised to Hong Kong in the Joint Declaration and the Basic Law had continued to be upheld.

The Financial Secretary (FS) presented the Budget for the financial year 2007-08 to the Legislative Council (LegCo).

FS proposed, among others, to revert the marginal bands and marginal rates for salaries tax to their 2002-03 levels; to increase the child allowance and the maximum amount of deduction for self-education expenses; to reduce the rate of stamp duty on transactions of properties with a value between \$1 million and \$2 million from 0.75% to a fixed amount of \$100.

FS also proposed, as one-off measures, to waive 50% of salaries tax and tax under personal assessment assessed for 2006-07, subject to a ceiling of \$15,000; and waive rates for the first two quarters of 2007-08, subject to a ceiling of \$5,000 per quarter for each rateable tenement.

The 2006 Economic Background and 2007 Economic Prospects was published along with the 2007-08 Budget. On Hong Kong's economic outlook for 2007, the Gross Domestic Product (GDP) growth was forecast at 4.5% to 5.5% in real terms, while the Composite Consumer Price Index (CPI) was forecast to increase by 1.5%.

5 Mar The Hong Kong Mortgage Corporation Limited (HKMC) launched a new retail bond issue with four series of notes under the \$20 Billion Retail Bond Issuance Programme.

7 Mar The Securities and Futures Commission (SFC) and the Hong Kong Exchanges and Clearing Limited (HKEx) published a joint policy statement which aimed at facilitating the listing of overseas companies by clarifying requirements in the Listing Rules and providing a clear roadmap for potential issuers and their advisers to refer to regarding key shareholder protection matters.

8 Mar The Asia Airfreight Terminal (AAT) celebrated the opening of its Terminal 2 which increased AAT's air cargo handling capacity to 1.5 million tonnes per year, more than doubling the capacity of its Terminal 1.

16 Mar The Government announced the 2007-08 Application List for the sale of Government land, which comprised 33 residential sites and 14 commercial/business sites of various sizes and at various locations.

The Fifth Session of the Tenth National People's Congress passed the Property Law and the Law on Corporate Tax. The Property Law, which took effect from 1 October 2007, confirmed the protection by law of the property of the state, collectives, individuals and other obligees. The Law on Corporate Tax would unify the corporate tax system for domestic and foreign-invested enterprises with effect from 1 January 2008. Among other things, the standard corporate tax rate would be set at 25%, and preferential tax rates would be available for small enterprises making minimal profits and which meet certain criteria and state-supported high-technological enterprises.

18 Mar The PBOC raised the one-year deposit interest rate by 27 basis points to 2.79% and the one-year lending rate by 27 basis points to 6.39%.

- 21 Mar The Fourth Digital Entertainment Leadership Forum was held, where overseas experts in digital entertainment shared their vision and experiences in digital content creation and distribution with the local practitioners.
- 24 Mar The second A380 route proving flight arrived at the Hong Kong International Airport (HKIA). The operations were smooth and the HKIA had affirmed its readiness to handle the new large aircraft.
- 28 Mar The HKEx signed an MOU with the Abu Dhabi Securities Market on cooperation and the exchange of information.
- 30 Mar The Urban Renewal Authority commenced the Kwun Tong Town Centre redevelopment project, which was the largest project ever undertaken by the Authority. It covered an area of about 5.3 hectares and affected over 4 700 residents and would serve to improve the living conditions of the residents, holistically regenerate the town centre, and provide impetus for further development of the district.

The Securities and Futures (Contracts Limits and Reportable Positions) (Amendment) Rules 2007, which increased the prescribed limits for Hang Seng China Enterprises Index futures and options contracts from 6 000 contracts per futures contract month or options contracts series to an aggregate delta limit of 12 000 applicable to all futures contract months and options series, commenced operation.

The SFC introduced a series of streamlined measures for the authorisation of UCITS III funds (funds domiciled in the European Union states and governed by the Undertakings of Collective Investment in Transferable Securities III issued by the European Commission) to facilitate the processing of UCITS III funds with special features.

- 1 Apr The arrangement under which the fiscal reserves placed with the Exchange Fund share in the investment return of the Fund changed. The return on the fiscal reserves for each year would be calculated on the basis of the average rate of return of the Exchange Fund's Investment Portfolio over the past six years, subject to a guarantee of a minimum return equivalent to the average yield of three-year Exchange Fund Notes for the previous year.

The Government lifted the general civil service open recruitment freeze (except for grades included in the Second Voluntary Retirement Scheme) as the target to reduce the size of the civil service establishment by 10% to around 160 000 by 2006-07 was achieved.

- 2 Apr The Office of the US Trade Representative released the 2007 National Trade Estimate Report on Foreign Trade Barriers. The report gave recognition to Hong Kong's continued efforts in protecting intellectual property rights and highlighted Hong Kong's efforts in removing service barriers and opening up markets.

The SFC, the Federation of Share Registrars, the Hong Kong Association of Banks and the Hong Kong Monetary Authority (HKMA) jointly launched a new measure to deter multiple applications for IPOs.

- 14 – 17 Apr The OGCIO collaborated with the Hong Kong Trade Development Council (HKTDC) to organise the International ICT Expo 2007. The event consisted of exhibition, conferences and forums that provided a platform for the industry to promote their ICT products and services. Business matching activities were also arranged for local, Mainland and overseas companies.
- 15 Apr The Film Development Committee, which was set up in November 2005, was expanded to form the high-level Hong Kong Film Development Council (HKFDC). The HKFDC, mainly comprising members from the film industry, was tasked to advise the Secretary for Commerce, Industry and Technology on the policy, strategy and institutional arrangement for the promotion and development of the film industry, as well as the use of public funds to support the industry.
- 16 Apr The “Mobile Enterprise 2007: Conference and Exhibition” was held to promote the development and wider adoption of mobile and wireless applications in various industries in Hong Kong.
- The third meeting of the “Mainland-Hong Kong Science and Technology Co-operation Committee” was held in Beijing. The Committee agreed to formulate a new mechanism for processing applications for setting up state key laboratories by Hong Kong universities and research institutes, and to organise large-scale events in 2007 to promote technological exchange and cooperation between Hong Kong and the Mainland.
- The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.
- 17 Apr A co-operation agreement was signed between the Commerce, Industry and Technology Bureau (CITB) and the Ministry of Information Industry on a framework for collaboration covering the areas of IT, telecommunications and technology.
- 18 Apr The Government, in collaboration with the Travel Industry Council of Hong Kong, the Hong Kong Tourism Board and the Consumer Council, announced a series of measures for enhancing the promotion of Honest and Quality Tourism to protect the consumer interests of Mainland visitors in Hong Kong.
- 20 Apr A new statutory regime for the revision of accounts and reports under the Companies Ordinance (Cap. 32) came into operation, providing an avenue for companies to voluntarily revise their accounts that might not comply with statutory requirements, thus helping to improve the integrity of financial reporting of companies, upgrading corporate governance and enhancing the protection of shareholders.
- 24 Apr The Spectrum Policy Framework, which aimed to provide the communications industry with greater clarity and predictability of spectrum management decisions, and policy guidance for the regulator in making regulatory decisions, was announced. As a guiding principle under the Framework, market-based approach should be used to manage radio spectrum in Hong Kong.
- 26 Apr The Telecommunications Authority published its first Spectrum Release Plan on the radio spectrum that might be made available to the market for the next three years through an open bidding or tendering process.

- 1 May The Employees' Compensation (EC) Insurance Residual Scheme, acting as a market of last resort to assist employers who have difficulties finding EC insurance cover, was launched.
- 4 May The HKMA announced that all 72 Hong Kong incorporated authorised institutions were reporting their capital adequacy positions under the newly implemented revised capital adequacy framework set out in the Banking (Capital) Rules, which took effect on 1 January 2007.
- 8 May The Government held the first land auction of 2007-08. A site in West Kowloon Reclamation Area with site area of 8 060 m² for residential use was sold for \$4 billion.
- 10 – 11 May At the Pan-Pearl River Delta (PRD) Customs Trade Facilitation Forum cum Regional Customs Commissioners' Joint Conference, Customs Administrations of the Mainland, Hong Kong and Macao issued a Joint Declaration for strengthening Customs cooperation and speeding up cross-boundary clearance in support of economic development in the Pan-PRD region. A Letter of Intent was also signed to cover eight cooperation projects.
- 11 May The China Banking Regulatory Commission promulgated through its notice the widening of the scope of investment allowed under the overseas wealth management business provided by the Mainland commercial banks on behalf of their clients. The investment scope was expanded to include equity investments, subject to certain conditions.
- The LegCo Finance Committee approved a sum of \$1,565 million for replacing the air traffic control system. The new system, which would be put into operation in late 2012, would be able to handle the projected traffic up to 2025.
- 15 May The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.
- 16 May The LegCo approved a ten-year increment scheme for the Sewage Charge, thus affirming its support for the application of the "polluter pays" principle to sewage services. Starting from 1 April 2008, the Sewage Charge would gradually increase at a rate of 9.3% per annum for ten consecutive years.
- 18 May The Government published the First Quarter Economic Report 2007. The Report pointed out that the Hong Kong economy continued to show broad-based expansion, with GDP growing solidly by 5.6% in real terms in the first quarter over a year earlier. The strong growth momentum was underpinned by the notable growth in exports of both goods and services amidst surging intra-regional trade and the brisk expansion of both offshore trade and inbound tourism. Locally, consumption spending continued to display strength on the back of rising income, improving job market and generally buoyant stock market activity and investment expenditure also grew moderately further.

In the May update of the economic forecast for 2007, the forecast growth rate in real terms of GDP was maintained at 4.5% to 5.5%, same as the forecast first released in the Budget. Meanwhile, the forecast rate of increase in the Composite CPI was kept at 1.5%.

- 19 May The PBOC raised the one-year deposit interest rate by 27 basis points to 3.06% and the one-year lending rate by 18 basis points to 6.57%.
- 21 May A co-operation agreement between CITB and Shenzhen Municipal Government on “Shenzhen-Hong Kong Innovation Circle” was signed.
- 23 May The Import and Export (Amendment) Ordinance 2007 was enacted to provide for the necessary regulation making powers for implementing the electronic advance cargo information system which aimed at facilitating customs clearance of road cargoes as well as the movement of transshipment cargoes that involve inter-modal transfer (e.g. from land to air).
- 25 May The LegCo Finance Committee approved funding of \$100 million to support the operation of the Hong Kong Design Centre over five years to promote the importance of design and innovation.
- 28 May The Government launched a public consultation on a proposal on an environmental levy on plastic shopping bags. The proposal was in line with the “polluter pays” principle, and aimed to reduce the indiscriminate use of plastic shopping bags through a direct economic disincentive. The proposal received overwhelming support from the public, and the Government gazetted the Product Eco-responsibility Bill in December 2007, which included the introduction of environmental levy on plastic shopping bags in prescribed retailers as the first producer responsibility scheme.
- 28 – 30 May Hong Kong co-organised the Sixth Management Seminar for the Heads of the National Statistical Offices in Asia and the Pacific with the United Nations Statistical Institute for Asia and the Pacific. The seminar aimed at strengthening the capability of national statistical offices in the area of leadership and management in information technology to facilitate enhancement of official statistical work in support of social and economic development.
- 29 May The Lantau Development Task Force released the Revised Concept Plan for Lantau (the Revised Plan) under which the overall planning vision for the island remained unchanged, i.e. to focus the development of major economic infrastructure and urban development in North Lantau whilst protecting the other areas of scenic and high ecological values in Lantau for nature conservation and environmentally sustainable development of recreational/tourism uses.
- 30 May The HKMA issued a non-statutory guideline on the application of the Banking (Disclosure) Rules which came into effect on 1 January 2007. The issuance of the Guideline completed the introduction of the new disclosure regime for authorised institutions that was established by the Rules.
- Moody’s indicated it would review Hong Kong’s long-term foreign-currency and long-term local-currency ratings, both at “Aa3”, for possible upgrade.
- 1 Jun Invest Hong Kong launched a major investment promotion campaign targeting private-owned enterprises (POEs) in high growth regions across Mainland China. The three-year campaign, ‘On Your Marks, Get-set Go’, would focus on seven key provinces – Zhejiang, Jiangsu, Shandong, Liaoning, Sichuan, Guangdong and Fujian – and aimed to provide POEs with the information and tools to expand internationally using Hong Kong as their gateway.

The 7th meeting of the Hong Kong-Zhuhai-Macao Bridge Advance Work Co-ordination Group (AWCG) was held in Guangzhou. AWCG members discussed and reviewed the progress of the studies on financing options and the arrangement of separate locations for boundary crossing facilities.

CE officiated at the Grand Opening of the HKIA's new passenger terminal.

The first phase of the Unsolicited Electronic Messages Ordinance, which regulated the use of unscrupulous techniques to reach out to a large number of recipients and fraud and other illicit activities related to the sending of multiple commercial electronic messages, came into force.

4 Jun Hong Kong hosted the 58th General Meeting of the Baltic and International Maritime Council (BIMCO) which was attended by BIMCO delegates from more than 40 countries.

5 Jun The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.

8 – 12 Jun CE led a delegation of government officials and business leaders to attend the Fourth Pan-PRD Regional Cooperation and Development Forum and Trade Fair in Changsha, Hunan.

11 Jun The SFC announced a set of initiatives to streamline the licensing procedures for overseas fund managers, which include expediting the licensing process for firms that are already registered as investment managers or advisors in specified overseas countries, and simplifying the licensing process for overseas hedge fund firms wishing to operate in Hong Kong.

The Government signed an agreement with the Hong Kong Polytechnic University to launch the Hong Kong Maritime Scholarship Scheme. The Scheme aimed to attract local and Mainland talents to take up maritime related post-graduate programmes in Hong Kong, and then joining Hong Kong's shipping and maritime industry.

15 Jun The Government introduced the Mandatory Provident Fund Schemes (Amendment) Bill 2007 into the LegCo. The Bill sought to further enhance the effectiveness and efficiency of the Mandatory Provident Fund (MPF) System. One of the major proposals was to include housing allowance and benefits in the definition of “relevant income” for the purpose of calculating the MPF contributions to rectify the irregularities that some employers deliberately designate a portion of their employees’ income as housing allowance to evade or reduce their responsibilities for making MPF contributions.

20 Jun The European Commission published its ninth report on the HKSAR. The report pointed out that in general the principle of “One Country, Two Systems” had been respected and was working well for the people of Hong Kong. It also commented, among others, that Hong Kong maintained its position as a regional hub for finance, trading, logistics and transport services.

The China Securities Regulatory Commission announced the Provisional Rules for Qualified Domestic Institutional Investors (QDIIs) Investing in Overseas Securities and a related Notice, which widened the scope of investment of QDII

- fund management companies and securities firms.
- 22 Jun The second meeting of the Hong Kong/Guangdong Expert Group on Co-operation in Informatisation under the Hong Kong/Guangdong Co-operation Joint Conference was held in Hong Kong to further promote co-operation in informatisation between the two places. Following the meeting, three co-operation agreements in the areas of software outsourcing, open source software as well as digital home and digital entertainment were signed between the industries of the two places.
- 25 Jun The HKEx launched the Electronic Disclosure Project which allowed straight-through publication of issuer documents on the HKEx website and made publishing fully paid announcements in local newspapers optional for issuers.
- The Government launched the one-year pilot Transport Support Scheme to encourage needy unemployed and low-income employees living in remote districts (viz. Tuen Mun, Yuen Long, North and Islands) to find jobs and work across districts.
- 27 Jun The HKMC announced the launch of US\$3 billion Medium Term Note Programme. This would help to set a quasi-sovereign benchmark for Hong Kong to further promote the development of the regional bond market. The multi-currency feature of the Programme would enable the HKMC to issue notes in major currencies to meet the demands of both domestic and overseas investors.
- 29 Jun The Government and the Central People's Government signed the Supplement IV to the CEPA. From 1 January 2008, the Mainland would implement 40 liberalisation measures in 28 service areas, including 17 existing CEPA service areas and 11 new ones. In addition, with effect from 1 July 2007, the number of products with CEPA rules of origin agreed was increased to 1 465.
- The Tenth Standing Committee of the National People's Congress passed the Law on Labour Contract, which governed the principles of establishing labour contracts, the content of labour contracts, the responsibilities of employers and employees, as well as certain specific issues like collective contracts and non-full time employment. The Law on Labour Contract would take effect from 1 January 2008.
- 30 Jun The US State Department published its tenth US Hong Kong Policy Act Report. The report gave an overall positive assessment of the developments in Hong Kong over the past ten years. It recognised that Hong Kong remained an international city and one of the most open, thriving and prosperous economies in the world. It affirmed Hong Kong's autonomy, rule of law and, respect for fundamental civil rights and human freedom.
- 1 Jul The Government Secretariat was reorganised. After the reorganisation, there were 12 bureaux in the Government Secretariat, with the net addition of one, being the Labour and Welfare Bureau.
- The Shenzhen Bay Port (SBP), Shenzhen Bay Bridge and Kong Sham Western Highway were opened to traffic. They served as Hong Kong's fourth vehicular boundary crossing. The SBP adopted a completely new clearance mode of "co-location", providing convenient, fast and efficient services to cross-boundary vehicles and passengers.

- 3 Jul The HKEx and the Moscow Interbank Currency Exchange signed an MOU on cooperation and the exchange of information.
- 5 Jul The Copyright (Amendment) Ordinance 2007 was passed into law. The Amendment Ordinance further enhanced Hong Kong's copyright protection regime.
- 6 Jul The LegCo Finance Committee approved the 2007-08 Civil Service Pay Adjustment which took retrospective effect on 1 April 2007. The adjustment rates ranged from 4.62% to 4.96%.
- The LegCo Finance Committee also approved the 2007 Civil Service Starting Salaries Adjustments which increased the starting pay of some entry ranks by one to five pay points. The adjustment took effect on 1 August 2007.
- The LegCo Finance Committee approved the Government's proposal to inject \$300 million into the Film Development Fund (FDF) to expand its scope to finance the provision of funding support for small-to-medium budget film productions. The FDF would also finance projects and activities that were conducive to the long-term of the Hong Kong film industry.
- 8 Jul The HKIA won the Air Transport Research Society's 2007 Asia-Pacific Airport Efficiency Excellence Award after receiving the top score in a field of over 30 major Asian airports. The airport was also awarded the Best International Airport Prize by a panel of travel industry experts and over 100 000 individual votes in the 2007 TravelWeekly (Asia) Industry Awards.
- 9 Jul The new ten-dollar polymer note was put into circulation.
- 12 Jul The first issue of renminbi bonds in Hong Kong was issued.
- The Treasury Markets Association launched a daily price fixing for renminbi denominated bonds issued in Hong Kong.
- 13 Jul Fitch upgraded Hong Kong's long-term foreign-currency rating from "AA-" to "AA", with "Stable" outlook. Fitch also affirmed Hong Kong's long-term local-currency rating at "AA+" with a "Stable" outlook.
- The Mandatory Provident Fund Schemes Authority launched a web-based Fee Comparative Platform to facilitate comparison of fees and charges of MPF funds.
- 16 Jul Following the release of results of the 2006 Population By-census, the Government announced an updated set of population projections for the period 2007-2036. The Hong Kong resident population was projected to increase at an average annual rate of 0.7%, from 6.86 million in mid-2006 to 8.57 million in mid-2036. The population was expected to remain on an ageing trend with the proportion of the population aged 65 and over projected to rise markedly, from 12% in 2006 to 26% in 2036. Meanwhile, the proportion of the population aged under 15 would decrease gradually from 14% to 12%.
- The Financial Reporting Council came into full operation and commenced receiving and handling complaints. The Council, established under the Financial

Reporting Council Ordinance (Cap. 588), was tasked to investigate irregularities concerning auditors and reporting accountants of listed entities and to enquire into non-compliance matters regarding financial statements of listed entities.

18 Jul With the approval of the FS and following consultation with the note issuing banks (NIBs), the HKMA announced an additional policy requirement relating to the continuing authorisation of banks as NIBs.

The Greater PRD Business Council Joint Investment and Trade Promotion Sub-group, in conjunction with Invest Hong Kong, organised the first POEs study mission to Hong Kong.

19 Jul The SFC released its annual Fund Management Activities Survey which showed that the combined fund management business in Hong Kong recorded a 36% year-on-year increase to \$6,154 billion as at end-2006.

20 Jul The Mainland's Ministry of Commerce, having discussed with the Food and Health Bureau, decided to increase the number of live pig agents from one to three with a view to ensuring the stable supply of live pigs from the Mainland to Hong Kong.

21 Jul The PBOC raised the one-year deposit interest rate by 27 basis points to 3.33% and the one-year lending rate by 27 basis points to 6.84%.

23 Jul The Mainland promulgated the Catalogue of Restricted Products for Processing Trade and related control measures, which took effect from 23 August 2007. Apart from adding 1 853 new 10-digit tariff code items to the restricted category for processing trade, the Mainland requested cash payment of customs duty deposit from enterprises carrying out processing trade of restricted products in the eastern region.

25 Jul The China Insurance Regulatory Commission promulgated the Provisional Measures for the Administration of Overseas Investment of Insurance Fund, which relaxed the limit of insurance funds that could be invested outside the Mainland to 15%.

26 Jul The UK Foreign and Commonwealth Office presented to UK parliament the 21st Six-monthly Report on Hong Kong covering the period January to June 2007. The Report also took a look back over the past ten years. The Report commented that in spite of the unforeseen economic challenges, Hong Kong had adapted, recovered and continued to prosper. It also stated that Hong Kong has made a reality of "One Country, Two Systems", and that Hong Kong remained a free and open society with an independent judiciary, and impartial and meritocratic civil service.

Standard & Poor (S&P) upgraded Hong Kong's foreign-currency and local-currency rating outlooks from "Stable" to "Positive". S&P also affirmed Hong Kong's long-term foreign-currency and long-term local-currency ratings at "AA".

Moody's upgraded Hong Kong's long-term foreign-currency and long-term local-currency ratings from "Aa3" to "Aa2", with "Stable" outlook.

27 Jul Hong Kong and the US exchanged letters of understanding on cooperation on the

US Secure Freight Initiative (SFI) for Hong Kong to participate in an SFI pilot in a limited capacity. The pilot helped detect and interdict illicit trafficking of special nuclear material and other radioactive material destined for the US.

Hong Kong Dragon Airlines Limited (Dragonair) was voted, for the sixth consecutive year, “Best Airline - China” in a large scale annual survey undertaken by Skytrax Research in the UK involving over 14 million voters of over 90 nationalities from August 2006 to June 2007.

30 Jul The Task Force to Support the Processing Trade, convened by the Commerce and Economic Development Bureau (CEDB), was set up. It comprised representatives from trade associations, industry support organisations and Government Bureaux and Departments. The purpose was to put together resources from various fronts with a view to providing more proactive and efficient assistance to the trade affected by changes in the Mainland’s processing trade policy.

31 Jul An opening ceremony was held at the Hong Kong Heritage Discovery Centre to signify the commencement of the Government Wi-Fi Programme. The Centre was the first Government site that provides Wi-Fi facilities for free trial use by the public.

2 Aug CE and the Governor of Guangdong Province co-chaired the Tenth Plenary of the Hong Kong Guangdong Co-operation Joint Conference held in Hong Kong. The Hong Kong/Guangdong Expert Group on the Restructuring and Upgrading of the Processing Trade was formed to assist Hong Kong-owned enterprises in Guangdong to upgrade and restructure.

The Government announced the decision of adopting the dedicated corridor option for the Hong Kong section of the Guangzhou - Shenzhen - Hong Kong Express Rail Link (ERL). This would not only greatly reduce the traveling time between Hong Kong and Guangzhou, but also help strengthen Hong Kong's status as the regional transportation hub.

8 Aug The HKIA was voted, for the sixth time in seven years, the “World’s Best Airport” in a large scale annual survey undertaken by Skytrax Research in the UK.

11 – 13 Aug The “Good Luck Beijing – HKSAR 10th Anniversary Cup” was held to test as many elements of Olympic Games operations as possible to prepare for the 2008 Olympic and Paralympic Equestrian Event. There were a total of 37 overseas and local riders taking part in the competition. The Event received positive feedbacks from the International Olympic Committee, the Fédération Equestre Internationale, the Beijing Organizing Committee for the Games of the XXIX Olympiad and others.

15 Aug The second cross-boundary railway in Hong Kong, the Sheung Shui to Lok Ma Chau Spur Line commenced operation.

The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.

17 Aug The Government published the Half-yearly Economic Report 2007. The Report pointed out that the Hong Kong economy expanded briskly with GDP accelerating to a 6.9% growth in real terms in the second quarter over a year earlier.

Externally, exports of goods sustained strong performance, supported by the Mainland's vibrant trade flows on the back of a buoyant economy and the weakening of the US dollar. Meanwhile, exports of services continued to show distinct growth, underpinned by the surge in offshore trade, buoyant financial market activities and sustained expansion of inbound tourism. Domestically, consumption demand continued to rise markedly alongside better job prospects and improved financial positions of households.

In the August update of the economic forecast for 2007, the forecast growth rate in real terms of GDP was revised upward to 5% to 6%, from 4.5% to 5.5% in the May round. Meanwhile, the forecast rate of increase in the Composite CPI was maintained at 1.5%.

- 20 Aug The State Administration of Foreign Exchange announced the pilot scheme which would allow Mainland individuals to invest directly in securities in Hong Kong.
- 22 Aug The HKMC announced the introduction of a new mortgage product with a 75% loan-to-value ratio and enhancements of Risk-based Pricing Scheme and Loyalty Discount Scheme under the Mortgage Insurance Programme.
- The PBOC raised the one-year deposit interest rate by 27 basis points to 3.60% and the one-year lending rate by 18 basis points to 7.02%.
- 23 – 25 Aug The Secretary for Commerce and Economic Development (SCED) led a business delegation to Chenzhou, Hunan to explore the feasibility for Hong Kong processing trade enterprises in the PRD region to relocate their operations to Chenzhou.
- 26 Aug – 1 Sep The Privacy Commissioner for Personal Data launched the Privacy Awareness Week (PAW) 2007 on 26 August together with his counterparts from Australia, New Zealand and South Korea. PAW 2007 was the first joint promotional initiative organised by members of the Asia Pacific Privacy Authorities to raise awareness of the importance of protecting privacy in the Asia Pacific Region.
- 28 Aug The HKMA launched the inaugural issue of 15-year Exchange Fund Notes. The issuance of the 15-year Exchange Fund Notes followed the recommendation arising from the October 2006 review of the Exchange Fund Bills and Notes programme. The review recommended extension of the benchmark yield curve to beyond 10 years.
- 30 – 31 Aug The First Steering Committee Meeting of the International Civil Aviation Organisation Cooperative Arrangement for Preventing the Spread of Communicable Diseases through Air Travel was hosted by the Civil Aviation Department.
- 3 – 6 Sep The 14th Asian Aerospace International Expo and Congress was held. It comprised an international congress and a large-scale exhibition at the Asia World Expo, an aircraft static display at the cargo apron and Business Aviation Centre at the HKIA. This was the first time that such a large scale civil aviation expo had been held in Hong Kong. In connection with this event, the Civil Aviation Department and Airbus jointly arranged an Airbus A380 low level flypast through.
- 4 Sep Hong Kong remained the freest economy in the world, according to the 2007

Annual Report on the Economic Freedom of the World jointly released by the Fraser Institute of Canada, CATO Institute of the US and 70 other research institutes around the world.

- 5 Sep The Mainland issued a notice confirming that processing trade enterprises could pay the customs duty deposit in various forms, including cash and letter of guarantee, etc.
- 7 Sep The Government announced that it had increased its shareholding in HKEx to 5.88% of the share issue of HKEx. The holdings in HKEx would be retained by the Exchange Fund as a strategic asset in support of the maintenance of Hong Kong as an international financial centre.
- 8 – 9 Sep CE attended the 15th Asia-Pacific Economic Cooperation Economic Leaders' Meeting in Sydney, Australia.
- 9 – 12 Sep CE visited New Zealand to update the political and business leaders on the latest developments in Hong Kong and strengthen bilateral links.
- 12 Sep The HKMA re-appointed the Standard Chartered Bank (Hong Kong) Limited as the Settlement Institution for the Euro clearing system in Hong Kong for a second five-year period commencing March 2008.

The Home Affairs Bureau (HAB) launched a three-month public engagement exercise on the recommendation of the Consultative Committee (CC) on the Core Arts and Cultural Facilities of the West Kowloon Cultural District (WKCD). CC recommended in the report, inter alia, the construction of 15 performing arts venues, a cultural institution with museum function and an exhibition centre. The Economic Impact Assessment in the report revealed that the WKCD project would bring substantial tangible and intangible economic benefits to Hong Kong. In general, the public supported the early implementation of the project. In light of this, the Administration planned to introduce a bill on the establishment of the WKCD Authority into the LegCo in early 2008, and to seek LegCo's approval in mid-2008 for an upfront endowment of \$21.6 billion for the WKCD Authority to finance the capital costs of the project as recommended in the CC report.

- 14 Sep CE officially opened Phase 2 of the Hong Kong Science Park.
- 15 Sep The PBOC raised the one-year deposit interest rate by 27 basis points to 3.87% and the one-year lending rate by 27 basis points to 7.29%.
- 17 Sep The Planning Department (PD) commenced the consultancy study on the planning of the Frontier Closed Area. A total of 2 400 hectares of land would be excised from the existing Frontier Closed Area by stages from 2010 onwards, and the development potential and constraints of such area need to be examined in detail.

The "2007 Guangdong-Hong Kong Technology Cooperation Funding Scheme" invited applications. Launched in 2004, the Scheme aimed to enhance collaborations among research institutions and technology enterprises in Hong Kong and Guangdong. In 2007, the two sides earmarked a total of \$800 million to support R&D projects and introduced a new category of projects which would receive funding from both the governments of the HKSAR and Guangdong Province.

- 19 Sep The Ministry of Commerce, the CEDB and the Trade and Industry Department of the HKSAR jointly organised the "Business Forum on Supplement IV to CEPA" in Hong Kong to brief the Hong Kong business community on the implementation progress of CEPA and to assist them to make full use of the opportunities of the new liberalisation measures under the Supplement IV to the CEPA. The Forum, attended by representatives from 11 central ministries and 13 provincial/municipal governments, and about 400 traders and professionals, was officiated by the FS and the Vice Minister of Commerce.
- The HKMA announced that the Base Rate was adjusted downward by 50 basis points to 6.25%.
- Oasis Hong Kong Airlines Limited (Oasis) was awarded "Best New Service" and "Best Business Class Carrier" at the 2007 World Low Cost Airline Congress Awards, held in London.
- 21 Sep The Asian Financial Forum, one of the major activities to mark the 10th anniversary of the HKSAR, was held by the Financial Services and the Treasury Bureau and the HKTDC. The Forum, carrying the theme "Leveraging New Opportunities, Advancing Regional Stability", aimed to highlight Hong Kong's prestige as an international financial centre. More than 800 senior representatives from global institutional investors, financial services institutions, high-growth corporations, government finance ministries and financial regulators participated in the Forum.
- 25 Sep The HKMA announced the Hong Kong results of the Bank for International Settlements (BIS) triennial survey on the turnover of foreign exchange and derivatives. The BIS also released the preliminary global results on the same day. In the global results, Hong Kong, as in the last survey in 2004, ranked sixth in the global foreign exchange market, and seventh if including transactions in the OTC derivatives market.
- The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.
- 25 – 28 Sep SCED led a high-level Hong Kong business promotion delegation to Russia. The trip aimed to explore market opportunities in Russia for Hong Kong traders and promote the image of Hong Kong lifestyle products in Russia. During the visit, SCED also officiated at the first "Style Hong Kong in Moscow" Exposition organised by the HKTDC and promoted Hong Kong's advantages as a financial centre and a business and trade platform.
- 2 Oct Results of the Annual Survey of Companies in Hong Kong Representing Parent Companies Located outside Hong Kong conducted by Census and Statistics Department showed that Hong Kong remained a magnet for international companies to oversee their regional operations. The total number of regional operations in Hong Kong again reached an all-time high, with over 3 800 regional headquarters and offices in Hong Kong.
- 3 Oct The turnover of the Hong Kong stock market exceeded \$210 billion, the highest ever in history.
- 9 Oct The EU announced that it had reached agreement with the Mainland to implement a system of joint import surveillance for eight categories of textiles and clothing

(T&C) products originating in the Mainland for one year in 2008, upon elimination of the quantitative restrictions imposed by EU on Mainland's T&C products under the EU/Mainland MOU signed in 2005.

10 Oct CE delivered his 2007-08 Policy Address setting out the action plan of the Third Term Government of the HKSAR.

11 Oct The PD completed and promulgated the Hong Kong 2030: Planning Vision and Strategy. The Study provided a strategic planning framework to guide the future development of Hong Kong with respect to economic competitiveness, land use and infrastructure provision up to 2030 and beyond. One of its key recommendations was to develop a number of "New Development Areas" in the New Territories.

12 Oct The cross-sector Steering Committee on MICE (Meetings, Incentives, Conventions and Exhibitions) led by the FS and SCED held its first meeting to review and devise strategies for promoting the development of the MICE industry in Hong Kong. The Steering Committee comprises representatives from the Government as well as the convention and exhibition, tourism and hotel industries and training institutions, etc.

15 Oct The OFTA announced the auction result of the spectrum for CDMA2000 services, which was one of the major telecommunications standards in the world. The successful bidder was required to rollout the service on 20 November 2008 to provide seamless CDMA services in Hong Kong.

16 Oct The Government announced that the MTR Corporation Limited would proceed with the detailed design of the West Island Line.

17 Oct The Government released the Report on Further Development of the Political Appointment System to set out the way forward on the creation of two additional layers of politically appointed officials, namely, Deputy Directors of Bureau and Political Assistants to Directors of Bureau.

Hong Kong retained its position as Asia's second largest destination for foreign direct investment (FDI), according to the "World Investment Report 2007", released by the United Nations Conference on Trade and Development. FDI flows to Hong Kong in 2006 reached US\$42.9 billion. On a global scale, Hong Kong ranked the seventh in FDI inflows in 2006.

18 Oct The SFC issued guidelines to explain the key criteria under which managers of authorised funds who were SFC licensees or whose investment management functions were based in an Acceptable Inspection Regime (AIR) might delegate investment management functions to affiliates in non-AIR jurisdictions.

The Hang Seng Index broke 30 000 points for the first time in history.

23 Oct The Hong Kong dollar strengthened to 7.75 in late October, underpinned by equity-related inflows and market rumours on changes to the Linked Exchange Rate system. The HKMA sold 775 million of Hong Kong dollars against the US dollar on 23 October within the Convertibility Zone and sold another 8.6 billion Hong Kong dollars when the strong-side Convertibility Undertaking was triggered on 26 and 31 October. As a result, the Aggregate Balance increased to HK\$10.6

billion on 2 November from HK\$1.3 billion. After that, interbank interest rates eased across the board and the Hong Kong dollar exchange rate bounced away from the 7.75 level. The HKMA's statement denying any changes to the peg also helped stabilise the market.

- 25 Oct The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.
- 26 Oct Gazettal of West Island Line under the Railways Ordinance.
- The HKIA was voted, for the fifth consecutive year, the “TTG’s Best Airport award”, and Cathay Pacific Airways Limited voted “Airline of the Year” and “Best North Asian Airline” in the TTG Travel Awards 2007.
- 29 Oct Bank Negara Malaysia and the HKMA implemented a cross-border delivery-versus-payment link between Hong Kong’s US dollar real time gross settlement (RTGS) system and Malaysia’s Ringgit RTGS system.
- 30 Oct The Government had completed the mid-term review of the Wage Protection Movement for Cleaning Workers and Security Guards (WPM). The review showed mixed results. The Government would continue to promote the WPM, as well as studying various issues that need to be tackled in the possible introduction of a statutory minimum wage for cleaning workers and security guards.
- 31 Oct The Mainland promulgated the Industrial Catalogue for Foreign Investment (2007 Revision), which took effect from 1 December 2007.
- The World Economic Forum released its Global Competitiveness Report 2007-2008. Hong Kong ranked 12th, a slip of 2 places from last year.
- 1 Nov The HKMA announced that the Base Rate was adjusted downward by 25 basis points to 6%.
- 2 Nov The Government of the HKSAR and the Government of Luxembourg signed an agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital.
- The LegCo Finance Committee approved the raising of the financial ceiling of the delegated authority for the Government to create Category D items in the Capital Works Programme from \$15 million to \$21 million. The increase would help expedite the implementation of minor works projects.
- 6 Nov The Chief Executive in Council approved the Kai Tak Outline Zoning Plan, allowing this vast ex-airport site to be developed into an attractive place for public enjoyment. The Kai Tak Outline Zoning Plan No. S/K22/2 was authorised to serve as a basis for guiding the re-development.
- 7 Nov The Merchant Shipping (Prevention of Air Pollution) Regulation was passed by the LegCo. With this Regulation, Hong Kong fulfilled its international convention obligation to implement the latest emission standard adopted by the International Maritime Organization.
- 9 Nov The Government invited open tender for the development of a new cruise terminal at Kai Tak. The successful tenderer was expected to design, build and operate the

new cruise terminal for 50 years and begin operating the first berth in February 2012. The tender would close on 7 March 2008.

16 Nov Funding approval was obtained from the LegCo to implement an electronic advance cargo information system for customs clearance of road cargoes.

The Government published the Third Quarter Economic Report 2007. The report pointed out that the Hong Kong economy stayed vibrant, with GDP leaping 6.2% in real terms in the third quarter over a year earlier. Externally, exports of goods grew notably further with exports to the Mainland and many emerging markets continued to hold up well. Growth in exports of services accelerated further along with surging offshore trade, vibrant financial market activities and strong inbound tourism. Locally, consumption demand grew strongly on the back of upbeat improving labour market and rising household income and wealth. Investment expenditure expanded further with business sentiment continued to hold up well.

In the November update of the economic forecast for 2007, the forecast growth rate in real terms of GDP was 6%, the upper end of the range forecast of 5% to 6% in the August round. Likewise, the forecast rate of increase in the Composite CPI was revised upward to 2.0%, from 1.5% in the August round.

19 Nov The HKMA and the Financial Reporting Council (FRC) entered into a MOU, aiming to elaborate on the mechanisms for communication and information exchange between the HKMA and the FRC, and to enhance the cooperation and mutual assistance between the two parties.

20 Nov The SFC authorised the first Islamic fund for sale to retail investors in Hong Kong.

An IMF staff mission to Hong Kong welcomed the Government's policies to enhance competitiveness. It maintained its long-standing support for the authorities' commitment to the Linked Exchange Rate system, and concluded that the real value of the Hong Kong dollar was in line with economic fundamentals. The mission welcomed the initiatives taken by the Hong Kong and Mainland authorities to deepen financial integration, and considered that they would clearly benefit both economies.

26 Nov The PBOC raised the renminbi reserve requirement ratio by 0.5 percentage point.

30 Nov The LegCo Finance Committee approved an allocation of \$1 billion to launch a Fourth Matching Grant Scheme. The Scheme would be opened for application by the eight University Grants Committee-funded institutions and two self-financing local universities, namely the Open University of Hong Kong and the Hong Kong Shue Yan University, from 1 January 2008 to 28 February 2009 to match their eligible private donations.

The Patents (Amendment) Ordinance 2007 was passed into law. The Ordinance enabled Hong Kong, as a member of the WTO, to contribute towards early implementation of a WTO Protocol to facilitate access to medicines (particularly on the part of developing and least developed economies). It also gave Hong Kong added flexibility in sourcing pharmaceutical products required to address a public health crisis.

The Government and the European Commission held the first Structured Dialogue

meeting in Hong Kong. Both sides recognised the long-standing bilateral relations between the European Union and Hong Kong, and would continue to enhance understanding and cooperation on economic, trade and regulatory issues of mutual interest.

- 1 Dec The eligibility criteria of the Employees Retraining Scheme were relaxed to cover young people aged 15 to 29 and people with education level at sub-degree or below.
- 2 Dec The merger of the Mass Transit Railway and the Kowloon-Canton Railway (KCR) systems came into being, bringing overall benefits to the community as a whole. The Kowloon-Canton Railway Corporation granted a service concession with an initial term of 50 years to MTR Corporation Limited (MTRCL) to operate the KCR system. Upon the merger, the Chinese name of MTRCL was changed to “香港鐵路有限公司” and the railway fares were reduced.
- 3 Dec The HKEx and the Hochiminh Stock Exchange signed an MOU on cooperation and exchange of information.
- The HKEx announced the introduction of a framework for third party clearing service in its securities market to give exchange participants more flexibility in their business operation.
- The Telecommunications Authority issued a statement on the release of the spectrum in 2.3GHz and the 2.5GHz bands by auction for the provision of Broadband Wireless Access services in Hong Kong. The auction would take place in the fourth quarter of 2008.
- 5 Dec The HKEx and the Mongolian Stock Exchange signed an MOU on cooperation and the exchange of information.
- 10 Dec The eighth meeting of the Hong Kong-Guangdong Joint Working Group on Sustainable Development and Environmental Protection was held in Guangzhou to consider and review the implementation of environmental co-operation initiatives, and further agreed on the work plan for 2008. The meeting noted that good progress had been made on various areas of cooperation.
- 11 Dec The HKMA launched the electronic trading platform for Exchange Fund Bills and Notes (EFBNs) which provided the necessary infrastructure to support electronic trading of other bonds in addition to EFBNs and could be extended to cover other financial instruments available in the market. It enhanced the price transparency among the market players and streamlined the trading process.
- 11 – 16 Dec FS led a high-level business mission to India to foster closer economic relationship between Hong Kong and India. Accompanied by about 20 leaders from financial and professional service sectors, the FS visited the Indian financial centre Mumbai and the capital New Delhi.
- 12 Dec The HKMA announced that the Base Rate was adjusted downward by 25 basis points to 5.75%.
- 12 – 14 Dec SCED led a business delegation to Ganzhou, Jiangxi to explore the feasibility for

Hong Kong processing trade enterprises to relocate their operations to Ganzhou.

13 Dec The Treasury Markets Summit, jointly organised by the HKMA and the Treasury Markets Association, was held in Beijing.

14 Dec New provisions concerning non-Hong Kong companies (formerly known as oversea companies) in the Companies Ordinance (Cap. 32) came into operation. The amendments modernised the registration regime for non-Hong Kong companies in Hong Kong by simplifying the registration requirements and enhancing the disclosure requirements for these companies.

17 Dec The pilot of On-Board Trucker Information System (OBTIS) was launched. The pilot, which would involve 500 trucks, aimed to increase the competitiveness of the logistics industry through enhanced information interconnectivity along the supply chain, as well as more efficient fleet management.

18 Dec Hong Kong and Shenzhen Governments signed an agreement "Co-operation Agreement on Recently Initiated Major Infrastructural Projects" and agreed to establish a new "Hong Kong-Shenzhen Joint Task Force on Boundary District Development" to explore the feasibility of developing the Lok Ma Chau Loop on the basis of mutual benefit, and steer further studies and planning on other cross-boundary issues. Moreover, an agreement for setting up a joint task force to foster closer co-operation between the HKIA and the Shenzhen International Airport was signed.

The Government announced that the MTR Corporation Limited would proceed with the preliminary planning of the South Island Line (East) Project.

20 Dec CE officiated at the Summit on Social Enterprise.

The HKMC signed a joint-venture agreement with Cagamas Berhad on the establishment of a joint-venture company to develop mortgage guarantee businesses in Malaysia and other Islamic countries, covering conventional and Shariah-compliant mortgage loans.

The HKEx announced measures to facilitate the listing of a wider range of Market Access Products, such as security listed on overseas exchanges and commodity asset or derivative contract, as a means to encourage financial innovation and to facilitate the development of our structured product market.

21 Dec The Hong Kong Shipping Register reached 36 million gross tonnage.

The Securities and Futures (Contracts Limits and Reportable Positions) (Amendment) (No. 2) Rules 2007, which enabled SFC to authorise Exchange Participants or their affiliates to exceed the statutory position limits for Hang Seng Index futures and options contracts and H-share Index futures and options contracts by up to 50% where this was required to serve clients' needs, commenced operation.

The SFC implemented a new measure to allow structured product issuers to apply for exemption from certain statutory reporting obligations, so as to reduce their compliance burden and to facilitate the issuance of structured products.

The Mainland promulgated the second batch of 2007 Catalogue of Prohibited

Products for Processing Trade, which consisted of 589 10-digit tariff code items and would take effect from 21 January 2008.

The PBOC raised the one-year deposit interest rate by 27 basis points to 4.14% and the one-year lending rate by 18 basis points to 7.47%.

- 22 Dec The Unsolicited Electronic Messages Ordinance came into full force. Following the implementation of the first phase on 1 June 2007, the second phase established the rules for sending commercial electronic messages. The registration of the do-not-call registers for fax messages commenced on the same day.
- 25 Dec The PBOC raised the renminbi reserve requirement ratio by 1 percentage point.
- 27 Dec The HKMC concluded its first cross-border asset purchase of residential mortgage loans in Korea, in the form of a private bilateral mortgage-backed securitisation, for a total amount of US\$700 million (HK\$5,460 million) from a major mortgage originating institution in Korea.
- 28 Dec The HKMC announced the expansion of the Mortgage Insurance Programme to cover loans secured by non owner-occupied residential properties, with a loan-to-value ratio up to 85%.
- 31 Dec CE officiated at the launching ceremony for digital terrestrial television (DTT) broadcasting.

The two domestic free television broadcasters, Asia Television Limited (ATV) and Television Broadcasts Limited (TVB), launched DTT broadcasting. Apart from simulcasting the existing four channels in both digital and analogue format, ATV and TVB both launched new High Definition TV and Standard Definition TV digital channels.

The Hong Kong stock market staged a robust performance in 2007, with market turnover and total market capitalisation both hitting record high. The total market capitalisation as at end-2007 was \$20.7 trillion, up 55% from end-2006.

The total net asset value of all MPF schemes reached \$264.8 billion, seven years after the launch of the MPF System on 1 December 2000. Besides, almost all MPF scheme sponsors/trustees had reviewed the fees and charges of their MPF funds during the year, resulting in a round of fee reduction initiatives.

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**Table 1 : Gross Domestic Product by expenditure component
(at current market prices)**

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>
	(\$Mn)					
Private consumption expenditure	795,948	765,248	777,141	782,984	748,402	719,873
Government consumption expenditure	116,550	119,993	120,172	128,866	131,291	130,151
Gross domestic fixed capital formation	388,731	325,328	347,375	333,044	286,025	261,576
<i>of which:</i>						
Building and construction	208,235	171,930	155,441	142,659	131,757	116,628
Machinery, equipment and computer software	165,177	141,349	180,204	180,011	144,832	136,537
Changes in inventories	-15,651	-10,612	14,399	-4,060	5,660	9,111
Total exports of goods	1,347,649	1,349,000	1,572,689	1,480,987	1,562,121	1,749,089
Imports of goods	1,408,317	1,373,500	1,636,711	1,549,222	1,601,527	1,794,059
Exports of services	262,099	276,385	315,012	320,799	347,836	362,420
Imports of services	194,245	185,174	192,427	194,180	202,494	203,400
GDP	1,292,764	1,266,668	1,317,650	1,299,218	1,277,314	1,234,761
<i>Per capita GDP (\$)</i>	<i>197,559</i>	<i>191,731</i>	<i>197,697</i>	<i>193,500</i>	<i>189,397</i>	<i>183,449</i>
GNP	1,317,362	1,291,436	1,326,404	1,327,761	1,282,966	1,263,252
<i>Per capita GNP (\$)</i>	<i>201,318</i>	<i>195,480</i>	<i>199,010</i>	<i>197,751</i>	<i>190,235</i>	<i>187,682</i>
Total final demand	2,895,326	2,825,342	3,146,788	3,042,620	3,081,335	3,232,220
Total final demand excluding re-exports ^(a)	1,952,900	1,886,157	2,048,719	1,983,301	1,923,623	1,896,483
Domestic demand	1,285,578	1,199,957	1,259,087	1,240,834	1,171,378	1,120,711
Private	1,107,816	1,014,313	1,078,515	1,053,973	986,542	939,104
Public	177,762	185,644	180,572	186,861	184,836	181,607
External demand	1,609,748	1,625,385	1,887,701	1,801,786	1,909,957	2,111,509

Definitions of Terms :

Total final demand	= private consumption expenditure + government consumption expenditure + gross domestic fixed capital formation + changes in inventories + total exports of goods + exports of services
Private sector domestic demand	= private consumption expenditure + gross domestic fixed capital formation by the private sector + changes in inventories
Public sector domestic demand	= government consumption expenditure + gross domestic fixed capital formation by the public sector
Domestic demand	= private sector domestic demand + public sector domestic demand
External demand	= total exports of goods + exports of services

**Table 1 : Gross Domestic Product by expenditure component
(at current market prices) (Cont'd)**

	(\$Mn)							
	<u>2004</u>	<u>2005</u>	<u>2006[#]</u>	<u>2007[#]</u>		<u>2007</u>		
					Q1 [#]	Q2 [#]	Q3 [#]	Q4 [#]
Private consumption expenditure	767,923	804,936	864,416	966,452	220,397	236,236	241,937	267,882
Government consumption expenditure	127,327	121,435	123,066	129,950	34,263	30,470	32,039	33,178
Gross domestic fixed capital formation	275,034	289,170	322,386	327,263	74,030	82,937	79,452	90,844
<i>of which:</i>								
Building and construction	107,692	105,993	105,960	112,263	27,807	29,106	27,399	27,951
Machinery, equipment and computer software	150,545	163,287	199,634	190,523	41,521	48,481	45,678	54,843
Changes in inventories	7,076	-4,761	-2,129	17,431	1,951	4,892	1,014	9,574
Total exports of goods	2,027,031	2,251,744	2,467,357	2,698,850	587,298	656,509	722,092	732,951
Imports of goods	2,099,545	2,311,091	2,576,340	2,852,522	621,522	702,713	749,449	778,838
Exports of services	429,584	495,394	565,054	645,276	147,521	148,319	171,992	177,444
Imports of services	242,507	264,237	287,900	320,102	71,141	76,645	86,490	85,826
GDP	1,291,923	1,382,590	1,475,910	1,612,598	372,797	380,005	412,587	447,209
<i>Per capita GDP (\$)</i>	<i>190,451</i>	<i>202,928</i>	<i>215,238</i>	<i>232,836</i>	--	--	--	--
GNP	1,315,333	1,384,238	1,503,258	N.A.	400,218	386,062	423,247	N.A.
<i>Per capita GNP (\$)</i>	<i>193,902</i>	<i>203,170</i>	<i>219,226</i>	<i>N.A.</i>	--	--	--	--
Total final demand	3,633,975	3,957,918	4,340,150	4,785,222	1,065,460	1,159,363	1,248,526	1,311,873
Total final demand excluding re-exports ^(a)	2,062,142	2,212,697	2,407,414	2,642,450	597,528	639,379	674,891	730,654
Domestic demand	1,177,360	1,210,780	1,307,739	1,441,096	330,641	354,535	354,442	401,478
Private	1,001,588	1,048,026	1,149,899	1,279,392	286,998	317,073	315,328	359,993
Public	175,772	162,754	157,840	161,704	43,643	37,462	39,114	41,485
External demand	2,456,615	2,747,138	3,032,411	3,344,126	734,819	804,828	894,084	910,395

Notes : (a) Re-export margin is nevertheless retained in the total final demand.

(#) Figures are subject to revision later on as more data become available.

(--) Not applicable.

N.A. Not available.

**Table 2 : Rates of change in chain volume measures of Gross Domestic Product
by expenditure component (in real terms)**

(%)

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>
Private consumption expenditure	-5.5	1.2	5.1	1.8	-0.9	-1.3
Government consumption expenditure	0.5	3.1	2.0	6.0	2.4	1.8
Gross domestic fixed capital formation	-7.6	-16.7	7.9	2.6	-4.7	0.9
<i>of which:</i>						
Building and construction	-1.6	-16.4	-7.9	-1.1	-1.3	-5.4
Machinery, equipment and computer software	-7.5	-17.6	27.3	6.2	-7.6	7.0
Total exports of goods	-4.6	3.6	16.9	-3.3	8.6	14.0
Imports of goods	-6.9	-0.1	18.4	-1.9	7.9	13.1
Exports of services	-3.9	8.9	13.4	6.4	11.1	7.6
Imports of services	2.8	-3.4	2.2	2.0	3.9	-2.2
GDP	-6.0	2.6	8.0	0.5	1.8	3.0
Per capita GDP (\$)	-6.8	1.6	7.0	-0.2	1.4	3.2
GNP	-4.1	2.6	6.6	2.0	0.1	4.9
Per capita GNP (\$)	-4.9	1.6	5.6	1.3	-0.3	5.1
Total final demand	-5.9	0.9	12.6	-0.7	5.0	7.9
Total final demand excluding re-exports ^(a)	-6.8	-1.3	9.8	0.3	2.0	3.1
Domestic demand	-7.7	-3.6	7.7	0.9	-0.7	-0.2
Private	-8.4	-4.6	9.5	0.5	-1.0	-0.5
Public	-3.5	2.4	-2.1	3.3	1.1	1.4
External demand	-4.5	4.5	16.3	-1.7	9.0	12.8

Notes : (a) Re-export margin is nevertheless retained in the total final demand.

(#) Figures are subject to revision later on as more data become available.

Table 2 : Rates of change in chain volume measures of Gross Domestic Product by expenditure component (in real terms) (Cont'd)

(%)

	<u>2004</u>	<u>2005</u>	<u>2006[#]</u>	<u>2007[#]</u>	<u>2007</u>				Average annual rate of change:	
					Q1 [#]	Q2 [#]	Q3 [#]	Q4 [#]	10 years 1997 to 2007 [#]	5 years 2002 to 2007 [#]
Private consumption expenditure	7.0	3.0	6.0	7.8	4.5	5.8	10.6	10.0	2.3	4.4
Government consumption expenditure	0.7	-3.2	0.1	2.3	2.3	2.9	1.5	2.3	1.6	0.3
Gross domestic fixed capital formation	2.5	4.1	7.0	6.0	2.8	10.0	1.0	10.4	-0.1	4.1
<i>of which:</i>										
Building and construction	-10.7	-7.6	-7.3	0.2	-2.2	6.5	-0.9	-2.3	-6.0	-6.2
Machinery, equipment and computer software	10.3	12.8	19.1	6.6	3.6	11.2	-0.4	11.9	4.9	11.1
Total exports of goods	14.9	10.4	9.3	7.2	6.6	10.1	6.4	5.9	7.5	11.1
Imports of goods	13.7	8.0	9.2	9.0	7.1	11.6	8.3	8.8	6.8	10.6
Exports of services	18.0	11.6	10.1	11.2	10.0	11.6	12.6	10.5	9.3	11.6
Imports of services	14.6	7.8	8.1	8.1	5.7	8.0	9.1	9.1	4.3	7.1
GDP	8.5	7.1	7.0	6.3	5.5	6.4	6.3	6.7	3.8	6.4
<i>Per capita GDP (\$)</i>	<i>7.6</i>	<i>6.6</i>	<i>6.3</i>	<i>5.2</i>	--	--	--	--	<i>3.1</i>	<i>5.8</i>
GNP	7.9	5.3	8.8	N.A.	9.1	9.0	6.0	N.A.	3.9 ^	5.4 ~
<i>Per capita GNP (\$)</i>	<i>7.0</i>	<i>4.8</i>	<i>8.1</i>	<i>N.A.</i>	--	--	--	--	<i>3.3 ^</i>	<i>4.9 ~</i>
Total final demand	11.8	7.7	8.4	8.0	6.5	9.6	7.7	8.1	5.4	8.7
Total final demand excluding re-exports ^(a)	8.9	5.4	7.3	7.3	4.2	7.7	7.3	9.6	3.5	6.4
Domestic demand	5.0	1.6	5.9	8.2	4.8	7.9	8.3	11.4	1.6	4.1
Private	6.2	3.0	7.5	9.3	5.8	8.7	9.5	12.9	2.0	5.0
Public	-1.2	-6.2	-4.0	-0.2	-1.3	1.4	-0.5	-0.1	-0.9	-2.1
External demand	15.4	10.6	9.4	7.9	7.2	10.3	7.5	6.7	7.8	11.2

Notes (cont'd) : (--) Not applicable.

N.A. Not available.

**Table 3 : Gross Domestic Product by economic activity
(at current prices)**

	<u>2002</u>		<u>2003</u>		<u>2004</u>		<u>2005</u>		<u>2006[#]</u>	
	\$Mn	% share	\$Mn	% share						
Agriculture and fishing	1,002	0.1	824	0.1	886	0.1	847	0.1	849	0.1
Mining and quarrying	136	*	116	*	72	*	100	*	93	*
Manufacturing	51,396	4.2	44,403	3.7	44,455	3.6	45,547	3.4	45,761	3.2
Electricity, gas and water	39,609	3.2	38,839	3.3	39,726	3.2	39,924	3.0	40,364	2.8
Construction	51,534	4.2	44,910	3.8	40,376	3.2	38,538	2.9	38,688	2.7
Services	1,079,476	88.3	1,062,714	89.2	1,119,304	89.9	1,207,873	90.6	1,298,692	91.2
<i>Wholesale, retail and import and export trades, restaurants and hotels</i>	<i>310,500</i>	<i>25.4</i>	<i>308,872</i>	<i>25.9</i>	<i>345,092</i>	<i>27.7</i>	<i>386,726</i>	<i>29.0</i>	<i>397,252</i>	<i>27.9</i>
<i>Transport, storage and communications</i>	<i>121,766</i>	<i>10.0</i>	<i>117,420</i>	<i>9.9</i>	<i>126,820</i>	<i>10.2</i>	<i>135,119</i>	<i>10.1</i>	<i>137,166</i>	<i>9.6</i>
<i>Financing, insurance, real estate and business services</i>	<i>247,045</i>	<i>20.2</i>	<i>251,085</i>	<i>21.1</i>	<i>266,855</i>	<i>21.4</i>	<i>294,260</i>	<i>22.1</i>	<i>356,371</i>	<i>25.0</i>
<i>Community, social and personal services</i>	<i>259,893</i>	<i>21.2</i>	<i>256,134</i>	<i>21.5</i>	<i>257,630</i>	<i>20.7</i>	<i>253,312</i>	<i>19.0</i>	<i>257,494</i>	<i>18.1</i>
<i>Ownership of premises</i>	<i>140,273</i>	<i>11.5</i>	<i>129,203</i>	<i>10.8</i>	<i>122,906</i>	<i>9.9</i>	<i>138,455</i>	<i>10.4</i>	<i>150,408</i>	<i>10.6</i>
GDP at factor cost	1,223,153	100.0	1,191,807	100.0	1,244,819	100.0	1,332,830	100.0	1,424,446	100.0
Taxes on production and imports	43,325		48,057		58,729		62,891		71,071	
Statistical discrepancy (%)	0.8		-0.4		-0.9		-0.9		-1.3	
GDP at current market prices	1,277,314		1,234,761		1,291,923		1,382,590		1,475,910	

Notes : Figures may not add up exactly to the total due to rounding.

(#) Figures are subject to revision later on as more data become available.

(*) Less than 0.05%.

**Table 4 : Rates of change in chain volume measures of Gross Domestic Product
by economic activity (in real terms)**

	(%)									
	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006[#]</u>	<u>2006</u>	<u>2007</u>		
							Q4 [#]	Q1 [#]	Q2 [#]	Q3 [#]
Agriculture and fishing	4.1	-1.1	-6.3	2.7	-1.0	-5.0	-5.8	-8.8	-7.0	-8.7
Mining and quarrying	-14.1	-11.3	2.3	-16.7	10.1	10.2	8.8	16.2	16.6	9.8
Manufacturing	-9.1	-10.0	-10.3	1.7	2.1	2.2	-1.4	-1.5	-2.3	-2.1
Electricity, gas and water	1.7	3.8	1.8	2.3	2.5	0.8	-4.0	1.6	2.5	0.2
Construction	-2.0	-1.9	-4.6	-9.3	-8.1	-9.8	-5.8	-6.2	3.7	-2.9
Services	1.7	2.7	4.3	9.9	7.5	7.2	7.4	6.7	7.1	7.3
<i>Wholesale, retail and import and export trades, restaurants and hotels</i>	0.3	4.4	8.9	15.1	14.1	8.8	8.7	6.9	7.5	7.5
<i>Transport, storage and communications</i>	1.9	6.4	0.6	13.9	7.4	6.8	7.2	4.0	4.8	6.7
<i>Financing, insurance, real estate and business services</i>	0.4	2.7	5.5	13.4	8.6	12.2	13.3	13.8	14.0	15.1
<i>Community, social and personal services</i>	4.0	-0.4	0.4	2.6	-0.1	1.8	1.9	1.6	1.4	0.8
<i>Ownership of premises</i>	3.4	1.8	2.8	1.5	2.9	2.4	2.0	2.1	2.1	2.2
Taxes on production and imports	-1.7	-0.2	2.6	12.3	0.8	7.2	19.3	11.9	10.6	23.4
GDP in chained (2005) dollars	0.5	1.8	3.0	8.5	7.1	7.0	6.6	5.5	6.4	6.3

Note : (#) Figures are subject to revision later on as more data become available.

**Table 5 : Balance of payments account by major component
(at current prices)**

(\$Mn)

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2006</u>	<u>2007</u>		
						Q4	Q1 [#]	Q2 [#]	Q3 [#]
Current account	96,800	128,240	122,512	156,933	178,166	55,740	64,056	26,944	63,711
Goods	-39,406	-44,970	-72,514	-59,347	-108,983	-25,243	-34,224	-46,204	-27,357
Services	145,342	159,020	187,077	231,157	277,154	79,963	76,380	71,674	85,502
Income	5,652	28,491	23,410	1,648	27,348	5,707	27,421	6,057	10,660
Current transfers	-14,787	-14,301	-15,461	-16,524	-17,353	-4,687	-5,521	-4,583	-5,094
Capital and financial account	-151,179	-179,086	-184,640	-182,431	-209,935	-72,345	-54,005	-40,224	-80,154
Capital and financial non-reserve assets (net change)	-169,720	-171,497	-159,155	-171,752	-163,199	-60,290	-41,633	-30,243	-66,271
Capital transfers	-15,686	-8,292	-2,561	-4,939	-2,900	-598	-1,196	3,730	7,048
Financial non-reserve assets (net change)	-154,033	-163,205	-156,594	-166,812	-160,300	-59,691	-40,437	-33,973	-73,319
<i>Direct investment</i>	-60,685	63,372	-91,038	49,996	635	34,794	1,299	23,778	22,187
<i>Portfolio investment</i>	-302,484	-264,619	-306,368	-245,017	-207,879	-198,191	5,840	-19,988	12,019
<i>Financial derivatives</i>	51,563	78,288	44,319	30,502	25,925	5,087	26,380	16,070	12,335
<i>Other investment</i>	157,573	-40,247	196,492	-2,294	21,019	98,618	-73,957	-53,832	-119,859
Reserve assets (net change) ^(a)	18,541	-7,589	-25,486	-10,679	-46,735	-12,056	-12,372	-9,981	-13,882
Net errors and omissions	54,379	50,846	62,128	25,498	31,769	16,605	-10,051	13,281	16,443
Overall balance of payments	-18,541	7,589	25,486	10,679	46,735	12,056	12,372	9,981	13,882

Notes : Figures may not add up exactly to the total due to rounding.

(a) A negative value for net change in reserve assets represents a net increase, and a positive value represents a net decrease.

(#) Figures are subject to revision later on as more data become available.

**Table 6 : Visible and invisible trade
(at current market prices)**

	(\$Mn)								
	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006[#]</u>	<u>2007[#]</u>	<u>2007</u>			
						Q1 [#]	Q2 [#]	Q3 [#]	Q4 [#]
Total exports of goods	1,749,089	2,027,031	2,251,744	2,467,357	2,698,850	587,298	656,509	722,092	732,951
Imports of goods	1,794,059	2,099,545	2,311,091	2,576,340	2,852,522	621,522	702,713	749,449	778,838
Visible trade balance	-44,970	-72,514	-59,347	-108,983	-153,672	-34,224	-46,204	-27,357	-45,887
	(-2.5)	(-3.5)	(-2.6)	(-4.2)	(-5.4)	(-5.5)	(-6.6)	(-3.7)	(-5.9)
Exports of services	362,420	429,584	495,394	565,054	645,276	147,521	148,319	171,992	177,444
Imports of services	203,400	242,507	264,237	287,900	320,102	71,141	76,645	86,490	85,826
Invisible trade balance	159,020	187,077	231,157	277,154	325,174	76,380	71,674	85,502	91,618
	(78.2)	(77.1)	(87.5)	(96.3)	(101.6)	(107.4)	(93.5)	(98.9)	(106.7)
Exports of goods and services	2,111,509	2,456,615	2,747,138	3,032,411	3,344,126	734,819	804,828	894,084	910,395
Imports of goods and services	1,997,459	2,342,052	2,575,328	2,864,240	3,172,624	692,663	779,358	835,939	864,664
Visible and invisible trade balance	114,050	114,563	171,810	168,171	171,502	42,156	25,470	58,145	45,731
	<5.7>	<4.9>	<6.7>	<5.9>	<5.4>	<6.1>	<3.3>	<7.0>	<5.3>

Notes : Figures in this table are reckoned on GDP basis.

(#) Figures are subject to revision later on as more data become available.

() As a percentage of the total value of imports of goods/services.

< > As a percentage of the total value of imports of goods and services.

**Table 7 : Total exports of goods by market
(in value terms)**

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>		<u>2007</u>			
	(% change)		(% change)		(\$Mn)		<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>
							(% change over a year earlier)			
All markets	11.7	15.9	11.4	9.4	9.2	2,687,513	9.0	11.7	8.2	8.2
Mainland of China	21.1	19.7	14.0	14.2	13.2	1,308,332	13.3	15.9	12.8	11.1
United States	-2.6	5.4	5.6	2.9	-0.8	368,202	1.9	1.3	-2.4	-3.0
Japan	12.3	14.4	10.3	1.6	-0.7	119,568	1.5	3.1	-6.2	-0.8
Germany	15.1	11.9	15.6	4.0	7.2	81,119	-0.9	10.9	12.1	6.6
United Kingdom	5.8	14.8	5.2	6.3	1.7	74,862	11.6	1.8	-5.3	1.6
Taiwan	22.2	16.2	2.7	3.3	1.6	52,934	3.9	10.0	-3.8	-2.1
Republic of Korea	16.9	24.0	9.5	7.5	2.0	52,930	-5.5	5.0	1.6	7.2
Singapore	13.0	22.0	6.8	4.4	3.8	50,450	4.7	3.9	2.4	4.3
Rest of the world	7.1	17.3	13.3	8.5	13.2	579,118	10.4	14.6	13.2	14.4

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

**Table 8 : Imports of goods by source
(in value terms)**

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>		<u>2007</u>			
	(% change)		(% change)		(\$Mn)	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	
						(% change over a year earlier)				
All sources	11.5	16.9	10.3	11.6	10.3	2,868,011	9.0	12.6	9.1	10.5
Mainland of China	9.6	16.9	14.3	13.7	11.5	1,329,652	10.3	16.5	8.7	10.7
Japan	17.2	19.7	0.1	4.5	7.2	287,329	8.2	9.3	5.6	5.9
Taiwan	8.0	22.8	9.4	15.9	5.2	205,102	0.4	4.8	7.0	7.8
Singapore	19.6	22.5	21.8	21.9	18.2	194,775	13.6	26.1	17.9	15.6
United States	7.9	13.4	6.5	3.6	12.3	138,768	16.3	12.6	8.3	12.6
Republic of Korea	15.0	15.0	2.6	16.1	-0.2	119,393	1.6	-2.9	7.5	-5.5
Rest of the world	12.1	13.6	8.4	7.6	10.7	592,991	8.4	8.4	10.5	15.1

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

**Table 9 : Retained imports of goods by end-use category
(in value terms)**

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>		<u>2007</u>			
	(% change)		(% change)		(\$Mn)	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	
						(% change over a year earlier)				
Overall	2.6	14.8	7.3	14.3	8.8	727,946	1.5	10.3	6.6	16.3
Foodstuffs	1.5	8.6	3.1	4.3	13.7	60,200	10.1	10.6	16.9	16.9
Consumer goods	-1.8	7.4	5.5	3.1	13.8	149,979	-4.1	8.8	20.7	32.1
Raw materials and semi-manufactures	10.7	17.6	4.2	8.8	14.4	268,729	8.4	19.3	17.7	11.8
Fuels	12.9	37.5	23.5	22.8	20.0	83,923	7.9	20.8	6.1	46.1
Capital goods	-6.6	13.3	10.8	33.2	-8.2	164,714	-8.5	-4.9	-19.7	0.9

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

**Table 10 : Exports and imports of services by component
(at current market prices)**

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006[#]</u>	<u>2007[#]</u>		<u>2007</u>			
	(% change)				(% change)	(\$Mn)	Q1 [#]	Q2 [#]	Q3 [#]	Q4 [#]
							(% change over a year earlier)			
Exports of services	4.2	18.5	15.3	14.1	14.2	645,276	13.2	14.0	15.5	13.9
Transportation	3.8	25.5	16.9	10.2	5.8	184,329	4.5	5.7	6.1	6.8
Travel	-4.4	26.1	14.2	12.9	18.6	107,226	18.0	15.2	18.3	22.1
Trade-related	12.2	12.6	10.7	9.9	12.8	201,053	12.5	13.5	13.5	11.8
Other services	-1.4	12.8	22.3	28.4	24.9	152,668	22.3	26.0	31.0	20.7
Imports of services	0.4	19.2	9.0	9.0	11.2	320,102	8.1	10.7	12.3	13.2
Transportation	7.8	29.4	20.3	10.9	10.1	99,372	5.6	9.9	10.3	14.1
Travel	-8.0	15.9	0.1	5.4	7.9	117,730	4.4	6.8	9.6	10.4
Trade-related	9.2	3.2	12.8	12.6	12.0	23,489	11.6	12.8	12.9	10.9
Other services	8.2	19.7	10.5	11.2	17.6	79,511	16.2	17.8	19.2	17.1
Net exports of services	9.4	17.6	23.6	19.9	17.3	325,174	18.4	17.9	18.9	14.6

Notes : Figures may not add up exactly to the total due to rounding.

(#) Figures are subject to revision later on as more data become available.

Table 11 : Incoming visitors by source

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2007</u>			
						<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>
<u>('000)</u>									
All sources	15 536.8	21 810.6	23 359.4	25 251.1	28 169.3	6 615.8	6 413.6	7 334.4	7 805.5
Mainland of China	8 467.2	12 245.9	12 541.4	13 591.3	15 485.8	3 778.2	3 321.5	4 212.4	4 173.6
South and Southeast Asia	1 359.6	2 077.7	2 413.0	2 659.7	2 888.1	566.3	749.1	649.4	923.3
Taiwan	1 852.4	2 074.8	2 130.6	2 177.2	2 238.7	525.7	540.4	608.1	564.5
Europe	780.8	1 142.7	1 398.0	1 548.2	1 772.2	413.8	419.5	413.4	525.5
Japan	867.2	1 126.3	1 210.8	1 311.1	1 324.3	337.3	305.2	333.5	348.3
United States	683.8	1 051.7	1 143.1	1 159.0	1 230.9	277.4	311.7	285.3	356.5
Others	1 525.8	2 091.7	2 522.6	2 804.5	3 229.2	716.9	766.0	832.3	913.9
<u>(% change over a year earlier)</u>									
All sources	-6.2	40.4	7.1	8.1	11.6	6.3	7.4	15.1	16.9
Mainland of China	24.1	44.6	2.4	8.4	13.9	5.2	6.6	20.6	23.0
South and Southeast Asia	-28.6	52.8	16.1	10.2	8.6	4.2	7.7	7.9	12.8
Taiwan	-23.7	12.0	2.7	2.2	2.8	-0.2	5.3	1.5	4.8
Europe	-28.0	46.3	22.3	10.7	14.5	17.7	15.1	14.8	11.3
Japan	-37.8	29.9	7.5	8.3	1.0	5.2	*	-1.0	*
United States	-31.7	53.8	8.7	1.4	6.2	5.1	3.8	3.2	12.0
Others	-20.8	37.1	20.6	11.2	15.1	14.2	13.0	17.5	15.6

Notes : Figures may not add up exactly to the total due to rounding.

(*) Change within $\pm 0.05\%$.

Table 12 : Property market

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Completion of new property by the private sector							
<i>('000 m² of internal floor area)</i>							
Residential property ^(a) (in units)	22 278	35 322	25 790	26 262	31 052	26 397	26 036
Commercial property	945	634	160	208	304	417	371
<i>of which :</i>							
Office space	737	428	96	76	166	299	280
Other commercial premises ^(b)	208	206	64	132	138	118	91
Industrial property ^(c)	300	191	62	45	29	15	1
<i>of which :</i>							
Industrial-cum-office premises	145	40	37	14	0	15	0
Conventional flatted factory space	31	4	19	30	3	0	1
Storage premises ^(d)	124	147	6	0	27	0	0
Production of public housing							
<i>(in units)</i>							
Rental housing flats ^(e)	14 267	26 733	40 944	47 590	20 154	13 948	20 947
Subsidized sales flats ^(e)	21 993	26 532	22 768	26 174	2 224	320	0
Building plans with consent to commence work in the private sector							
<i>('000 m² of usable floor area)</i>							
Residential property	1 472.0	1 692.8	1 142.7	1 002.5	790.0	1 038.4	530.0
Commercial property	395.7	287.5	337.5	265.0	365.3	200.0	161.3
Industrial property ^(f)	69.5	84.9	129.2	45.7	107.1	0.8	16.4
Other properties	201.5	125.8	240.2	75.0	109.3	444.2	407.1
Total	2 138.7	2 190.9	1 849.5	1 388.1	1 371.8	1 683.3	1 114.8
Agreements for sale and purchase of property							
<i>(Number)</i>							
Residential property ^(g)	85 616	77 087	65 340	69 667	72 974	71 576	100 630
Primary market	23 441	18 325	13 911	18 366	23 088	26 498	25 694
Secondary market	62 175	58 762	51 429	51 301	49 886	45 078	74 936
Selected types of non-residential properties ^(h)							
Office space	N.A.	N.A.	1 724	1 774	1 639	1 817	3 213
Other commercial premises	N.A.	N.A.	2 411	2 989	3 167	4 142	7 833
Flatted factory space	N.A.	N.A.	N.A.	N.A.	3 756	3 813	5 889

Notes : Figures may not add up exactly to the total due to rounding.

- (a) Figures before 2002 cover all completed residential premises to which either temporary or full Occupation Permits have been granted, as well as village type houses issued with Letters of Compliance. Property developments subject to a Consent Scheme need a Certificate of Compliance, Consent to Assign or Consent to Lease in addition to an Occupation Permit before the premises can be individually assigned. Village-type housing units are excluded as from 2002 and units issued with temporary Occupation Permits are also excluded as from 2004 onwards.

Residential premises here pertain to private residential units, excluding units built under the Private Sector Participation Scheme (PSPS), Home Ownership Scheme (HOS), Buy or Rent Option, Mortgage Subsidy Scheme, Sandwich Class Housing Scheme, Urban Improvement Scheme (UIS) and Flat-for-Sale Scheme. Figures from 2004 onwards also cover those private flats converted from subsidised flats.

- (b) These include retail premises and other premises designed or adapted for commercial use, with the exception of purpose-built offices. Car-parking space and commercial premises built by the Hong Kong Housing Authority and the Hong Kong Housing Society are excluded.
- (c) These include industrial-cum-office premises, but exclude specialised factory buildings which are developed mainly for own use.
- (d) These include storage premises at the container terminals and the airport.

Table 12 : Property market (Cont'd)

	<u>2005</u>	<u>2006</u>	<u>2007</u>		<u>2007</u>		
				Q1	Q2	Q3	Q4
Completion of new property by the private sector							
<i>('000 m² of internal floor area)</i>							
Residential property ^(a) (in units)	17 321	16 579	10 471	2 273	647	1 444	6 107
Commercial property	145	291	503	34	175	4	156
<i>of which :</i>							
Office space	34	108	320	10	165	0	145
Other commercial premises ^(b)	111	183	183	24	9	4	11
Industrial property ^(c)	17	27	16	0	0	2	14
<i>of which :</i>							
Industrial-cum-office premises	4	0	0	0	0	0	0
Conventional flatted factory space	0	0	16	0	0	2	14
Storage premises ^(d)	13	27	0	0	0	0	0
Production of public housing							
<i>(in units)</i>							
Rental housing flats ^(e)	24 691	4 430	4 795	4 795	0	0	0
Subsidized sales flats ^(e)	0	0	2 010	1 200	0	810	0
Building plans with consent to commence work in the private sector							
<i>('000 m² of usable floor area)</i>							
Residential property	550.7	706.7	956.1	48.7	300.4	471.6	135.5
Commercial property	481.9	468.4	327.5	127.6	46.1	45.4	108.4
Industrial property ^(f)	35.1	23.9	103.5	11.0	70.2	18.0	4.4
Other properties	408.0	199.2	207.7	71.9	44.9	40.4	50.5
Total	1 475.8	1 398.2	1 594.8	259.1	461.6	575.3	298.8
Agreements for sale and purchase of property							
<i>(Number)</i>							
Residential property ^(g)	103 362	82 472	123 575	23 328	30 293	29 421	40 533
Primary market	15 994	13 986	20 123	3 095	5 876	5 722	5 430
Secondary market	87 368	68 486	103 452	20 233	24 417	23 699	35 103
Selected types of non-residential properties ^(h)							
Office space	3 431	2 874	4 180	723	918	990	1 549
Other commercial premises	7 143	4 402	5 477	1 099	1 425	1 351	1 602
Flatted factory space	6 560	7 409	9 136	1 906	2 431	2 269	2 530

Notes (e) The Housing Authority's housing production figures have been revised as from 1998. The revision is to exhaustively cover all housing production and to count projects (including surplus HOS projects) which undergo transfer of usage at the time of disposal and according to their actual usage. Moreover, surplus HOS courts and blocks pending disposal are excluded from production statistics until they are disposed. Rental and sales flats projects of the Housing Society are included.

(f) These include multi-purpose industrial premises designed also for office use.

(g) The figures are derived from sale and purchase agreements of domestic units received for registration for the relevant periods. They generally relate to transactions executed up to four weeks prior to their submission for registration. Sales of domestic units refer to sale and purchase agreements with payment of stamp duty. These statistics do not include sales of units under the Home Ownership Scheme, the Private Sector Participation Scheme and the Tenants Purchase Scheme except those after payment of premium. Primary sales generally refer to sales from developers. Secondary sales refer to sales from parties other than developers.

(h) Timing of the figures for non-residential properties is based on the date on which the S&P Agreement is signed, which may differ from the date on which the Agreement is received for registration.

N.A. Not available.

Table 13 : Property prices and rentals

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
<u>(Index (1999=100))</u>							
Property price indices :							
Residential flats ^(a)	117.1	100.0	89.6	78.7	69.9	61.6	78.0
Office space ^(b)	134.5	100.0	89.9	78.7	68.4	62.5	99.3
Shopping space	128.3	100.0	93.6	86.8	85.0	85.5	119.3
Flatted factory space	131.8	100.0	91.2	82.0	74.8	71.7	88.6
Property rental indices ^(c) :							
Residential flats	112.6	100.0	98.1	95.4	83.4	73.6	77.7
Office space ^(b)	135.9	100.0	98.5	101.0	85.4	74.6	78.1
Shopping space	111.2	100.0	101.3	99.4	92.9	86.4	92.8
Flatted factory space	118.1	100.0	95.4	90.3	82.7	74.9	77.3
<u>(% change)</u>							
Property price indices :							
Residential flats ^(a)	-28.2	-14.6	-10.4	-12.2	-11.2	-11.9	26.6
Office space ^(b)	-36.9	-25.7	-10.1	-12.5	-13.1	-8.6	58.9
Shopping space	-27.6	-22.1	-6.4	-7.3	-2.1	0.6	39.5
Flatted factory space	-22.0	-24.1	-8.8	-10.1	-8.8	-4.1	23.6
Property rental indices ^(c) :							
Residential flats	-16.3	-11.2	-1.9	-2.8	-12.6	-11.8	5.6
Office space ^(b)	-13.3	-26.4	-1.5	2.5	-15.4	-12.6	4.7
Shopping space	-10.0	-10.1	1.3	-1.9	-6.5	-7.0	7.4
Flatted factory space	-10.9	-15.3	-4.6	-5.3	-8.4	-9.4	3.2

Notes : (a) Figures pertain to prices of existing flats traded in the secondary market, but not new flats sold in the primary market.

(b) Since 2000, price and rental indices for office space in the private sector have been recomputed according to the revised grading criteria for office space. Hence, the figures from 2000 onwards are not strictly comparable to those in the earlier years.

(c) All rental indices shown in this table have been adjusted for concessionary leasing terms such as provision of refurbishment, granting of rent-free periods, and waiver of miscellaneous charges, if known.

For residential property, changes in rentals cover only new tenancies for which rentals are freshly determined. For non-residential property, changes in rentals cover also lease renewals upon which rentals may be revised.

Table 13 : Property prices and rentals (Cont'd)

	<u>2005</u>	<u>2006</u>	<u>2007⁺</u>		<u>2007</u>		
				Q1	Q2	Q3 [#]	Q4 ⁺
<u>(Index (1999=100))</u>							
Property price indices :							
Residential flats ^(a)	92.0	92.7	103.4	96.6	100.3	104.0	112.6
Office space ^(b)	133.0	139.3	164.2	148.5	156.2	166.3	185.6
Shopping space	149.3	153.5	172.2	158.8	168.7	175.7	185.5
Flatted factory space	125.0	158.5	198.6	176.9	193.2	206.4	217.8
Property rental indices ^(c) :							
Residential flats	86.5	91.6	101.6	96.0	99.6	103.7	107.3
Office space ^(b)	96.4	117.4	131.9	125.8	129.6	133.4	138.9
Shopping space	100.5	104.3	112.1	108.1	109.9	113.3	117.1
Flatted factory space	82.6	91.0	99.9	96.7	99.2	101.5	102.1
<u>(% change over a year earlier)</u>							
Property price indices :							
Residential flats ^(a)	17.9	0.8	11.5	5.6	7.6	12.2	20.7 <89.9> {-33.6}
Office space ^(b)	33.9	4.7	17.9	13.4	12.0	15.6	30.1 <214.6> {-17.5}
Shopping space	25.1	2.8	12.2	4.7	9.2	14.2	20.4 <129.0> {-4.1}
Flatted factory space	41.1	26.8	25.3	22.6	25.0	25.5	27.6 <211.1> {25.5}
Property rental indices ^(c) :							
Residential flats	11.3	5.9	10.9	7.5	9.6	12.5	13.9 <49.2> {-22.8}
Office space ^(b)	23.4	21.8	12.4	14.3	10.4	10.9	14.2 <93.7> {-12.6}
Shopping space	8.3	3.8	7.5	4.7	6.9	8.8	9.5 <39.2> {-6.0}
Flatted factory space	6.9	10.2	9.8	12.1	10.0	9.5	7.8 <41.4> {-23.6}

Notes (cont'd) : (#) Figures for non-residential property are provisional.

(+) Provisional figures.

< > % change from the trough in 2003.

{ } % change from the peak in 1997.

Table 14 : Monetary aggregates

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
<u>(as at end of period)</u>							
Hong Kong dollar money supply (\$Mn) :							
M1	178,260	205,339	203,966	229,841	259,411	354,752	412,629
M2 ^(a)	1,828,691	1,923,481	1,987,963	1,998,774	1,984,049	2,107,269	2,208,591
M3 ^(a)	1,840,824	1,935,471	2,002,358	2,016,635	2,004,225	2,122,861	2,219,557
Total money supply (\$Mn)							
M1	197,666	225,156	243,847	258,056	295,650	413,423	484,494
M2	3,111,942	3,386,196	3,649,492	3,550,060	3,518,326	3,813,442	4,166,706
M3	3,168,199	3,434,467	3,692,753	3,594,130	3,561,852	3,858,044	4,189,544
Deposit ^(b) (\$Mn)							
HK\$	1,699,726	1,773,169	1,851,177	1,854,651	1,824,911	1,930,790	2,017,911
Foreign currency	1,300,302	1,477,448	1,676,670	1,551,852	1,492,631	1,636,227	1,848,145
Total	3,000,027	3,250,617	3,527,847	3,406,502	3,317,542	3,567,018	3,866,056
Loans and advances (\$Mn)							
HK\$	1,695,027	1,607,126	1,652,191	1,647,684	1,615,667	1,573,079	1,666,740
Foreign currency	1,609,400	1,205,784	809,259	537,301	460,659	462,000	488,964
Total	3,304,427	2,812,910	2,461,450	2,184,986	2,076,325	2,035,079	2,155,704
Nominal Effective Exchange Rate Indices (Jan 2000 = 100) ^{(c)(d)}							
Trade-weighted	103.4	100.9	101.7	104.7	104.0	100.7	98.3
Import-weighted	105.5	101.4	101.5	105.1	104.7	101.6	99.2
Export-weighted	101.3	100.4	101.9	104.3	103.3	99.8	97.3
<u>(% change)</u>							
Hong Kong dollar money supply :							
M1	-5.2	15.2	-0.7	12.7	12.9	36.8	16.3
M2 ^(a)	9.7	5.2	3.4	0.5	-0.7	6.2	4.8
M3 ^(a)	9.3	5.1	3.5	0.7	-0.6	5.9	4.6
Total money supply :							
M1	-5.0	13.9	8.3	5.8	14.6	39.8	17.2
M2	11.6	8.8	7.8	-2.7	-0.9	8.4	9.3
M3	10.3	8.4	7.5	-2.7	-0.9	8.3	8.6
Deposit ^(b)							
HK\$	9.5	4.3	4.4	0.2	-1.6	5.8	4.5
Foreign currency	12.2	13.6	13.5	-7.4	-3.8	9.6	13.0
Total	10.7	8.4	8.5	-3.4	-2.6	7.5	8.4
Loans and advances							
HK\$	-2.7	-5.2	2.8	-0.3	-1.9	-2.6	6.0
Foreign currency	-32.4	-25.1	-32.9	-33.6	-14.3	0.3	5.8
Total	-19.8	-14.9	-12.5	-11.2	-5.0	-2.0	5.9
Nominal Effective Exchange Rate Indices ^{(c)(d)}							
Trade-weighted	5.5	-2.4	0.8	2.9	-0.7	-3.2	-2.4
Import-weighted	7.8	-3.9	0.1	3.5	-0.4	-3.0	-2.4
Export-weighted	3.3	-0.9	1.5	2.4	-1.0	-3.4	-2.5

Definition of Terms :

The Hong Kong Dollar Money Supply is the Hong Kong dollar component of the respective monetary aggregate. Starting from April 1997, money supply definition has been revised to include short-term Exchange Fund placements of less than one month in the monetary aggregates. As such, figures at end-1997 cannot be compared with those at end-1996.

Total Money Supply:

- M1: Legal tender notes and coins with the public, plus customers' demand deposits with licensed banks.
- M2: M1 plus customers' savings and time deposits with licensed banks, plus negotiable certificates of deposit issued by licensed banks and held outside the monetary sector.
- M3: M2 plus customers' deposits with restricted licence banks and deposit-taking companies, plus negotiable certificates of deposit issued by such institutions and held outside the monetary sector.

Table 14 : Monetary aggregates (Cont'd)

	<u>2005</u>	<u>2006</u>	<u>2007</u>		<u>2007</u>		
				Q1	Q2	Q3	Q4
<u>(as at end of period)</u>							
Hong Kong dollar money supply (\$Mn) :							
M1	348,248	387,918	454,361	418,842	504,970	483,484	454,361
M2 ^(a)	2,329,669	2,777,823	3,281,335	2,948,372	3,193,184	3,404,795	3,281,335
M3 ^(a)	2,345,838	2,795,688	3,300,818	2,966,455	3,211,318	3,424,319	3,300,818
Total money supply (\$Mn)							
M1	434,684	491,657	616,727	534,416	643,417	633,039	616,727
M2	4,379,057	5,054,475	6,106,665	5,271,752	5,593,867	5,944,734	6,106,665
M3	4,407,188	5,089,884	6,140,076	5,302,225	5,624,184	5,976,046	6,140,076
Deposit ^(b) (\$Mn)							
HK\$	2,131,579	2,568,426	3,075,360	2,736,438	2,986,547	3,203,802	3,075,360
Foreign currency	1,936,322	2,188,993	2,793,856	2,236,227	2,342,046	2,490,305	2,793,856
Total	4,067,901	4,757,419	5,869,216	4,972,665	5,328,594	5,694,108	5,869,216
Loans and advances (\$Mn)							
HK\$	1,797,350	1,917,437	2,184,982	2,070,264	2,209,937	2,334,345	2,184,982
Foreign currency	514,637	550,392	776,960	601,228	648,896	707,994	776,960
Total	2,311,987	2,467,828	2,961,942	2,671,492	2,858,833	3,042,339	2,961,942
Nominal Effective Exchange Rate Indices (Jan 2000 =100) ^{(c)(d)}							
Trade-weighted	97.4	96.1	91.9	93.7	92.7	91.6	89.9
Import-weighted	98.1	96.8	92.5	94.3	93.5	92.2	90.4
Export-weighted	96.7	95.5	91.3	93.0	92.0	90.9	89.4
<u>(% change over a year earlier)</u>							
Hong Kong dollar money supply :							
M1	-15.6	11.4	17.1	17.4	42.9	31.7	17.1
M2 ^(a)	5.5	19.2	18.1	20.2	27.4	28.4	18.1
M3 ^(a)	5.7	19.2	18.1	20.1	27.3	28.3	18.1
Total money supply :							
M1	-10.3	13.1	25.4	21.7	43.8	34.6	25.4
M2	5.1	15.4	20.8	16.6	20.6	22.4	20.8
M3	5.2	15.5	20.6	16.5	20.5	22.3	20.6
Deposit ^(b)							
HK\$	5.6	20.5	19.7	21.7	29.8	31.2	19.7
Foreign currency	4.8	13.0	27.6	14.1	15.4	18.1	27.6
Total	5.2	17.0	23.4	18.2	23.1	25.1	23.4
Loans and advances							
HK\$	7.8	6.7	14.0	15.5	18.7	20.8	14.0
Foreign currency	5.3	6.9	41.2	12.2	16.8	25.0	41.2
Total	7.2	6.7	20.0	14.8	18.3	21.8	20.0
Nominal Effective Exchange Rate Indices ^{(c)(d)}							
Trade-weighted	-0.9	-1.3	-4.4	-4.0	-3.6	-4.4	-5.3
Import-weighted	-1.1	-1.3	-4.4	-4.0	-3.4	-4.5	-5.4
Export-weighted	-0.6	-1.2	-4.4	-4.1	-3.8	-4.4	-5.1

- Notes : (a) Adjusted to include foreign currency swap deposits.
- (b) Starting from April 1997, deposits include short-term Exchange Fund placements of less than one month. As such, figures at end-1997 cannot be compared with those at end-1996.
- (c) Period average.
- (d) The Effective Exchange Rate Indices (EERIs) from January 2000 onwards are compiled on the basis of the average merchandise trade pattern from 1999 to 2000. The EERIs for the earlier periods are compiled on the basis of the average merchandise trade pattern in a much earlier period from 1991 to 1993, and have been re-scaled to the new base period for linking up with the new index series.
- (--)

Table 15 : Rates of change in business receipts indices for service industries/domains

(%)

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2007</u>		
					Q1-Q3 [#]	Q1	Q2	Q3 [#]
Wholesale trade	-5.0	4.7	5.6	7.9	8.6	7.3	9.3	9.0
Retail trade	-2.3	10.8	6.8	7.3	11.2	9.4	9.1	15.1
Import/export trade	6.5	12.4	10.6	10.2	8.2	7.5	8.9	8.2
Restaurants	-9.7	10.1	6.0	9.5	12.9	11.8	11.6	15.4
Hotels	-19.7	39.4	22.1	13.8	14.7	15.9	12.5	15.7
Transport ^(a)	0.5	22.8	17.8	10.6	9.4	5.9	10.2	11.7
Storage	-4.5	17.0	10.4	10.2	18.1	18.4	25.0	11.7
Communications	-2.4	1.0	5.1	0.8	7.9	5.8	8.0	9.7
Banking	*	4.4	10.9	19.5	35.7	27.3	32.4	47.7
Financing (other than banking)	17.3	33.2	14.3	47.9	62.5	35.0	54.3	99.6
Insurance	19.1	22.3	16.0	21.3	26.3	16.0	21.8	42.1
Real estate	6.2	13.5	16.0	-0.4	29.0	25.7	33.6	27.7
Business services	0.5	8.3	4.9	19.6	12.9	14.8	12.1	11.8
Film entertainment	2.3	3.7	5.0	1.7	6.1	4.5	4.6	9.1
Tourism, convention and exhibition services	-7.3	26.5	12.9	14.0	16.3	14.7	16.6	17.6
Computer and information services	5.7	20.5	23.4	9.7	3.8	3.7	6.7	1.6

Notes : (a) Including business receipts from the Airport Authority Hong Kong.

(#) Revised figures.

(*) Change within $\pm 0.05\%$.

Table 16 : Labour force characteristics[#]

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2007</u>			
						Q1	Q2	Q3	Q4
<u>(%)</u>									
Labour force participation rate	61.4	61.3	61.0	61.3	61.4	61.2	61.4	61.6	61.3
Seasonally adjusted unemployment rate	7.9	6.8	5.6	4.8	4.0	4.3	4.2	4.1	3.4
Underemployment rate	3.5	3.2	2.7	2.4	2.2	2.2	2.2	2.2	2.1
<u>('000)</u>									
Population of working age	5 652.4	5 733.1	5 801.4	5 845.9	5 930.1	5 899.0	5 928.6	5 935.1	5 957.6
Labour force	3 472.5	3 515.9	3 538.1	3 581.4	3 640.5	3 611.9	3 640.7	3 658.4	3 651.1
Persons employed	3 197.4	3 276.5	3 340.8	3 410.2	3 495.0	3 459.4	3 485.0	3 502.2	3 533.3
Persons unemployed	275.1	239.4	197.3	171.2	145.6	152.5	155.7	156.3	117.8
Persons underemployed	121.4	114.1	96.3	86.2	79.4	80.6	81.2	80.5	75.5
<u>(% change over a year earlier)</u>									
Population of working age	0.6	1.4	1.2	0.8	1.4	1.5	1.7	1.3	1.2
Labour force	*	1.3	0.6	1.2	1.7	1.7	2.7	1.3	1.0
Persons employed	-0.7	2.5	2.0	2.1	2.5	2.5	3.4	2.0	2.0
Persons unemployed	8.4	-13.0	-17.6	-13.2	-15.0	-14.1	-11.7	-12.0	-23.3
Persons underemployed	16.9	-6.0	-15.6	-10.5	-7.8	0.6	-12.7	-4.1	-13.7

Notes : (#) Figures enumerated from the General Household Survey have been revised to take into account the recent enhancements in the estimation method and the results of the 2006 Population By-census, which provide a benchmark for revising the population figures compiled since the 2001 Population Census.

(*) Change within $\pm 0.05\%$.

Table 17 : Employment in selected major economic sectors

Major economic sector	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2006</u>	<u>2007</u>			No.	
	(% change)					<u>Dec</u>	<u>Mar</u>	<u>Jun</u>	<u>Sep</u>		(% change over a year earlier)
Manufacturing	-9.0	-10.3	-3.0	-2.0	-2.5	-4.8	-1.7	-2.3	-2.6	155 968	
<i>of which :</i>											
Printing, publishing and allied industries	-6.4	-5.2	-1.2	-3.1	2.0	3.7	2.3	1.6	-1.0	37 181	
Food, manufacturing	0.9	-2.6	3.9	5.4	5.2	4.3	10.3	8.8	1.2	23 061	
Wearing apparel, except footwear	-19.3	-11.6	-0.8	-4.7	-10.5	-19.0	-16.5	-17.6	-12.4	16 168	
Textiles	-1.1	-16.8	-11.1	0.5	-4.4	-7.0	1.8	-4.8	-7.0	17 856	
Electronics	-13.1	-18.9	-2.3	-4.7	-12.9	-16.1	-14.6	-7.1	-1.6	12 042	
Transport equipment, manufacturing	-5.3	-0.4	-3.3	8.6	3.6	0.7	10.2	5.6	3.2	10 048	
Wholesale, retail, import/export trades, restaurants and hotels	-2.3	-3.0	2.9	2.6	1.9	2.3	1.9	1.6	1.7	1 056 855	
<i>of which :</i>											
Wholesale, retail and import/export trades	-1.6	-1.9	2.1	2.3	1.1	1.8	1.2	1.2	0.9	819 555	
Restaurants and hotels	-4.8	-7.3	6.0	3.6	5.1	4.3	4.4	3.0	4.9	237 300	
Transport, storage and communications	-1.8	-4.4	3.7	2.6	1.1	1.7	1.1	3.1	2.2	189 812	
<i>of which :</i>											
Land transport	-0.3	0.5	-2.2	-1.5	0.3	1.2	0.2	0.8	0.9	38 074	
Water transport	1.0	-3.6	0.1	-0.3	-4.4	-2.1	-3.7	-0.2	-1.8	25 619	
Air transport	0.7	-0.4	5.2	6.2	5.4	4.4	4.0	4.5	4.5	29 931	
Services incidental to transport	1.5	-4.0	11.3	8.0	3.1	2.8	2.8	5.7	4.2	60 283	
Financing, insurance, real estate and business services	-1.3	-1.9	3.6	4.4	5.0	5.8	5.1	5.7	6.0	509 257	
<i>of which :</i>											
Financial institutions	-5.6	-6.5	1.1	4.7	5.9	8.1	7.9	9.1	9.3	146 983	
Insurance	0.3	1.2	2.4	5.9	-1.2	-1.0	-0.7	1.6	1.8	29 540	
Real estate	5.2	0.7	2.2	6.8	5.3	3.2	2.0	4.5	5.2	102 648	
Business services except machinery and equipment rental and leasing	-1.2	-0.2	6.0	2.9	5.3	6.7	5.5	4.7	4.8	229 265	
Community, social and personal services	5.9	2.9	3.2	4.5	3.6	3.1	2.9	3.6	2.2	465 356	
<i>of which :</i>											
Sanitary and similar services	13.8	6.0	1.5	2.4	2.5	3.7	3.1	7.0	-2.1	58 085	
Education services	2.5	2.9	1.8	1.8	4.9	4.5	3.7	4.6	2.5	141 926	
Medical, dental and other health services	3.2	-0.3	2.5	1.6	4.0	4.5	5.9	5.5	4.8	84 457	
Welfare institutions	11.9	13.9	2.1	-0.4	1.5	*	1.3	0.7	2.4	53 657	
Civil Service^(a)	-3.7	-2.4	-3.8	-2.7	-1.3	-1.1	-0.8	-0.5	-0.2	153 768	

Notes : (a) These figures cover only those employed on Civil Service terms of appointment. Judicial officers, consultants, contract staff and temporary staff not appointed on Civil Service terms are not included.

(*) Change within $\pm 0.05\%$.

Table 18 : Number of workers engaged at building and construction sites

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2006</u> Dec	Mar	<u>2007</u> Jun	Sep
<u>(number)</u>									
Building sites									
Private sector	40 017	33 892	33 619	31 556	30 993	29 556	28 123	30 100	29 016
Public sector ^(a)	11 727	16 183	13 325	10 135	7 643	6 850	8 394	7 567	7 117
Sub-total	51 744	50 074	46 944	41 690	38 636	36 406	36 517	37 667	36 133
Civil engineering sites									
Private sector	2 869	2 755	2 564	2 198	1 569	1 434	1 674	1 766	1 395
Public sector ^(a)	18 611	17 466	16 772	15 378	12 661	13 164	12 175	11 665	11 645
Sub-total	21 480	20 221	19 336	17 576	14 230	14 598	13 849	13 431	13 040
Total	73 223	70 295	66 280	59 266	52 865	51 004	50 366	51 098	49 173
<u>(% change over a year earlier)</u>									
Building sites									
Private sector	-1.3	-15.3	-0.8	-6.1	-1.8	-2.5	-12.5	-2.9	-7.2
Public sector ^(a)	-31.8	38.0	-17.7	-23.9	-24.6	-19.0	1.0	-3.3	-6.2
Sub-total	-10.4	-3.2	-6.3	-11.2	-7.3	-6.1	-9.8	-3.0	-7.0
Civil engineering sites									
Private sector	9.0	-4.0	-6.9	-14.3	-28.6	-8.1	5.0	3.5	-9.4
Public sector ^(a)	-6.6	-6.2	-4.0	-8.3	-17.7	-6.8	-5.1	-0.7	-9.7
Sub-total	-4.8	-5.9	-4.4	-9.1	-19.0	-6.9	-4.0	-0.2	-9.7
Total	-8.8	-4.0	-5.7	-10.6	-10.8	-6.3	-8.3	-2.2	-7.7

Note : (a) Including the Mass Transit Railway Corporation Limited and the Airport Authority Hong Kong.

Table 19 : Average labour earnings by major economic sector

(\$)

Major economic sector	2002	2003	2004	2005	2006	2006	2007		
						Q4	Q1	Q2	Q3
Wholesale, retail and import/export trades	12,500 (-1.6) <1.4>	12,300 (-1.5) <1.1>	12,400 (0.4) <0.9>	13,300 (7.3) <6.3>	13,800 (4.1) <2.0>	14,100 (5.1) <2.9>	15,600 (0.3) <-1.4>	12,800 (2.5) <1.3>	13,500 (3.5) <1.9>
Restaurants and hotels	8,700 (-4.2) <-1.2>	8,100 (-6.2) <-3.7>	8,100 (-0.1) <0.4>	8,300 (1.9) <0.9>	8,500 (2.6) <0.6>	8,700 (8.1) <5.8>	9,400 (4.1) <2.3>	8,400 (4.8) <3.5>	8,500 (3.7) <2.2>
Transport, storage and communications	18,900 (-0.2) <2.9>	18,500 (-1.7) <0.9>	18,300 (-1.3) <-0.9>	19,200 (5.0) <4.1>	19,600 (2.1) <0.1>	21,400 (5.8) <3.6>	20,600 (4.1) <2.4>	19,100 (1.9) <0.7>	19,200 (3.9) <2.3>
Financing, insurance, real estate and business services	18,800 (-2.2) <0.8>	18,600 (-1.4) <1.2>	18,500 (-0.1) <0.4>	19,100 (2.8) <1.8>	20,100 (5.6) <3.6>	21,200 (6.3) <4.1>	23,500 (5.9) <4.2>	19,800 (4.1) <2.9>	19,100 (5.4) <3.8>
Community, social and personal services	19,800 (-1.3) <1.8>	18,900 (-4.7) <-2.2>	18,400 (-2.6) <-2.2>	18,000 (-2.2) <-3.1>	17,900 (-0.1) <-2.0>	18,100 (-0.1) <-2.2>	17,900 (0.7) <-1.0>	17,800 (-0.1) <-1.3>	19,000 (4.6) <3.0>
Manufacturing	11,800 (-1.2) <1.9>	11,400 (-3.0) <-0.4>	11,300 (-0.6) <-0.2>	11,600 (1.8) <0.9>	11,700 (1.4) <-0.6>	11,700 (0.8) <-1.3>	13,100 (1.3) <-0.4>	11,700 (3.1) <1.9>	11,300 (3.8) <2.2>
All sectors surveyed	15,300 (-1.1) <2.0>	15,000 (-1.8) <0.8>	14,900 (-0.7) <-0.2>	15,400 (3.5) <2.6>	15,800 (2.4) <0.4>	16,300 (4.0) <1.8>	17,500 (2.4) <0.7>	15,300 (2.9) <1.7>	15,600 (4.6) <3.0>

Notes : () % change over a year earlier in money terms.

< > % change over a year earlier in real terms.

The rates of change in real terms are derived from the Real Indices of Payroll per Person Engaged. As from 2006, the Indices are derived by deflating the Nominal Indices of Payroll per Person Engaged by the 2004/2005-based Composite CPI. To facilitate comparison, Real Indices of Payroll per Person Engaged prior to 2006 have been re-scaled using the 2004/2005-based Composite CPI.

**Table 20 : Rates of change in wage indices by
selected major economic sector**

(%)

Selected major economic sector	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2006</u>	<u>2007</u>		
						Dec	Mar	Jun	Sep
<u>(in money terms)</u>									
Wholesale, retail and import/export trades	-0.6	-1.7	-1.6	1.6	1.1	1.6	1.7	2.2	2.0
Restaurants and hotels	-2.6	-4.1	-2.2	*	1.0	0.9	1.4	2.2	1.0
Transport services	0.6	-1.9	-1.0	1.0	-0.6	0.4	0.3	1.6	2.0
Financing, insurance, real estate and business services	-0.8	-0.1	-0.5	*	3.2	3.4	3.1	3.5	3.0
Personal services	-1.5	-3.1	1.3	-1.5	2.5	6.1	5.7	6.2	6.5
Manufacturing	-1.4	-2.7	-1.3	1.2	2.9	3.2	1.6	2.6	1.6
All sectors surveyed	-1.0	-1.9	-1.1	0.8	1.5	2.0	2.0	2.6	2.3
<u>(in real terms)</u>									
Wholesale, retail and import/export trades	1.7	0.4	-1.7	0.4	-0.6	-0.3	-0.5	1.4	1.0
Restaurants and hotels	-0.4	-2.1	-2.3	-1.3	-0.8	-0.9	-0.7	1.4	*
Transport services	2.9	0.1	-1.0	-0.2	-2.3	-1.5	-1.8	0.8	1.0
Financing, insurance, real estate and business services	1.5	2.0	-0.6	-1.2	1.5	1.5	0.9	2.7	2.0
Personal services	0.8	-1.1	1.3	-2.7	0.7	4.2	3.4	5.4	5.4
Manufacturing	0.8	-0.7	-1.4	-0.1	1.1	1.2	-0.5	1.8	0.6
All sectors surveyed	1.3	0.2	-1.2	-0.4	-0.3	0.1	-0.2	1.8	1.3

Notes : The rates of change in real terms are compiled from the Real Wage Indices. As from 2006, the Indices are derived by deflating the Nominal Wage Indices by the 2004/2005-based CPI(A). To facilitate comparison, Real Wage Indices prior to 2006 have been re-scaled using the 2004/2005-based CPI(A).

(*) Change within $\pm 0.05\%$.

Table 21 : Rates of change in prices

(%)

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
GDP deflator	0.8	-4.5	-3.6	-1.9	-3.5	-6.2	-3.5	-0.1
Domestic demand deflator	-1.2	-3.1	-2.6	-2.3	-4.9	-4.2	0.1	1.2
Consumer Price Indices ^(a) :								
Composite CPI	2.8	-4.0	-3.8	-1.6	-3.0	-2.6	-0.4	1.0
CPI(A)	2.6	-3.3	-3.0	-1.7	-3.2	-2.1	*	1.1
CPI(B)	2.8	-4.7	-3.9	-1.6	-3.1	-2.7	-0.5	1.0
CPI(C)	3.2	-3.7	-4.5	-1.5	-2.8	-2.9	-0.9	0.8
Unit Value Indices :								
Domestic exports	-2.8	-2.4	-1.0	-4.7	-3.3	0.2	1.5	2.2
Re-exports	-3.9	-2.8	-0.1	-2.0	-2.7	-1.5	1.1	1.2
Total exports of goods	-3.8	-2.7	-0.2	-2.3	-2.7	-1.4	1.2	1.3
Imports of goods	-4.9	-2.0	0.8	-3.1	-3.9	-0.4	2.9	2.7
Terms of Trade Index	1.2	-0.7	-1.0	0.9	1.2	-1.0	-1.7	-1.4
Producer Price Index for all manufacturing industries	-1.8	-1.6	0.2	-1.6	-2.7	-0.3	2.2	0.8
Construction Labour and Material Cost Index	7.5	1.4	1.8	0.3	-0.3	-1.0	-1.2	-2.1
Tender Price Indices :								
Public sector building projects	9.1	-4.4	-13.1	-8.5	-11.7	-0.3	-1.5	1.4
Public housing projects	9.0	-3.3	-11.9	-15.1	-9.6	-10.0	3.5	7.7

Notes : (a) From October 2005 onwards, the year-on-year rates of change in the Consumer Price Indices are derived from the 2004/05-based CPI series. For the earlier periods, the year-on-year rates of change are derived from the CPIs with old base period.

(#) Figures are subject to revision later on as more data become available.

(*) Change within $\pm 0.05\%$.

Table 21 : Rates of change in prices (Cont'd)

	(%)							
	2006	2007	2007				Average annual rate of change:	
			Q1	Q2	Q3	Q4	10 years 1997 to 2007	5 years 2002 to 2007
GDP deflator	-0.3 #	2.8 #	1.2 #	1.8 #	3.3 #	4.7 #	-2.0 #	-1.5 #
Domestic demand deflator	1.9 #	1.9 #	0.3 #	1.0 #	1.5 #	4.3 #	-1.3 #	0.2 #
Consumer Price Indices ^(a) :								
Composite CPI	2.0	2.0	1.7	1.3	1.6	3.5	-0.8	0.4
CPI(A)	1.7	1.3	0.3	0.7	0.9	3.1	-0.7	0.4
CPI(B)	2.1	2.2	2.0	1.3	1.7	3.6	-0.9	0.4
CPI(C)	2.2	2.7	2.9	1.8	2.3	3.7	-0.8	0.4
Unit Value Indices :								
Domestic exports	-2.1	0.8	0.4	0.6	0.8	1.0	-1.2	0.5
Re-exports	1.1	2.4	2.8	2.1	2.1	2.8	-0.7	0.9
Total exports of goods	1.0	2.3	2.7	2.0	2.0	2.7	-0.8	0.8
Imports of goods	2.1	2.3	2.6	1.9	1.9	2.8	-0.4	1.9
Terms of Trade Index	-1.1	0.1	0.1	0.1	0.2	-0.1	-0.4	-1.1
Producer Price Index for all manufacturing industries	2.3	N.A.	2.5	2.6	2.4	N.A.	-0.3 ^	0.4 ~
Construction Labour and Material Cost Index	0.1	N.A.	4.0	2.2	-0.7	N.A.	1.5 ^	-0.9 ~
Tender Price Indices :								
Public sector building projects	5.0	N.A.	15.0	17.7	20.6	N.A.	-1.1 ^	-1.6 ~
Public housing projects	11.2	N.A.	21.9	18.4	16.6	N.A.	-0.6 ^	0.2 ~

Notes (cond't) : (^) Average annual rate of change for the 10-year period 1996-2006.

(~) Average annual rate of change for the 5-year period 2001-2006.

N.A. Not available.

Table 22 : Rates of change in Composite Consumer Price Index

(%)

	Weight	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
All items	100.0	2.8	-4.0	-3.8	-1.6	-3.0	-2.6	-0.4
Food	26.94	1.9	-1.8	-2.2	-0.8	-2.1	-1.5	1.0
<i>Meals bought away from home</i>	<i>(16.86)</i>	<i>2.2</i>	<i>-1.2</i>	<i>-0.9</i>	<i>-0.3</i>	<i>-1.5</i>	<i>-1.5</i>	<i>0.2</i>
<i>Food, excluding meals bought away from home</i>	<i>(10.08)</i>	<i>1.5</i>	<i>-2.8</i>	<i>-4.2</i>	<i>-1.7</i>	<i>-3.1</i>	<i>-1.7</i>	<i>2.5</i>
Housing ^(a)	29.17	4.7	-5.1	-8.2	-3.1	-5.7	-4.8	-5.2
<i>Private housing rent</i>	<i>(23.93)</i>	<i>5.5</i>	<i>-6.1</i>	<i>-9.8</i>	<i>-2.9</i>	<i>-6.5</i>	<i>-6.3</i>	<i>-6.6</i>
<i>Public housing rent</i>	<i>(2.49)</i>	<i>-3.4</i>	<i>1.4</i>	<i>1.1</i>	<i>-8.3</i>	<i>-2.7</i>	<i>9.1</i>	<i>2.5</i>
Electricity, gas and water	3.59	1.4	-0.4	3.6	-1.9	-7.0	1.4	11.4
Alcoholic drinks and tobacco	0.87	6.6	1.2	-0.9	3.3	2.4	0.1	*
Clothing and footwear	3.91	-0.8	-20.6	-10.1	-4.6	0.7	-2.7	6.4
Durable goods	5.50	0.2	-6.3	-4.6	-7.1	-6.3	-6.4	-2.2
Miscellaneous goods	4.78	2.6	-0.7	0.9	1.3	1.7	2.3	3.6
Transport	9.09	3.9	0.5	1.0	0.4	-0.6	-0.4	0.4
Miscellaneous services	16.15	2.7	-1.3	-0.2	0.5	-2.3	-3.2	-0.2

Notes : From October 2005 onwards, the year-on-year rates of change in the Composite Consumer Price Index are derived from the 2004/05-based CPI series. For the earlier periods, the year-on-year rates of change are derived from the CPIs with old base period. The weights quoted in this table correspond to that in the new series.

(a) Apart from "Private housing rent" and "Public housing rent", the "Housing" section also includes "Management fees and other housing charges" and "Materials for house maintenance".

(*) Change within $\pm 0.05\%$.

N.A. Not available.

Table 22 : Rates of change in Composite Consumer Price Index (Cont'd)

	Weight	(%)								
		<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2007</u>				Average annual <u>rate of change:</u>	
					Q1	Q2	Q3	Q4	10 years 1997 to 2007	5 years 2002 to 2007
All items	100.0	1.0	2.0	2.0	1.7	1.3	1.6	3.5	-0.8	0.4
Food	26.94	1.8	1.7	4.3	2.9	2.8	4.8	6.7	0.2	1.4
<i>Meals bought away from</i>	<i>(16.86)</i>	<i>0.9</i>	<i>1.3</i>	<i>2.5</i>	<i>1.8</i>	<i>2.0</i>	<i>2.6</i>	<i>3.7</i>	<i>0.2</i>	<i>0.7</i>
<i>Food, excluding meals bought</i> <i>away from home</i>	<i>(10.08)</i>	<i>3.2</i>	<i>2.5</i>	<i>7.1</i>	<i>4.4</i>	<i>4.1</i>	<i>8.2</i>	<i>11.6</i>	<i>0.3</i>	<i>2.7</i>
Housing ^(a)	29.17	0.1	4.7	2.0	2.2	1.0	0.7	4.2	-2.2	-0.7
<i>Private housing rent</i>	<i>(23.93)</i>	<i>-0.1</i>	<i>5.6</i>	<i>4.0</i>	<i>5.6</i>	<i>2.0</i>	<i>2.3</i>	<i>5.9</i>	<i>-2.5</i>	<i>-0.8</i>
<i>Public housing rent</i>	<i>(2.49)</i>	<i>0.2</i>	<i>0.1</i>	<i>-17.7</i>	<i>-31.7</i>	<i>-10.5</i>	<i>-17.8</i>	<i>-10.8</i>	<i>-2.0</i>	<i>-1.6</i>
Electricity, gas and water	3.59	4.1	2.1	-0.7	-1.3	-2.2	-2.7	3.4	1.3	3.6
Alcoholic drinks and tobacco	0.87	0.4	-3.7	-1.2	-3.9	-0.1	-1.1	0.5	0.8	-0.9
Clothing and footwear	3.91	2.0	1.0	4.1	7.2	3.9	3.7	2.0	-2.8	2.1
Durable goods	5.50	-3.2	-6.4	-4.7	-5.8	-4.6	-4.2	-4.0	-4.7	-4.6
Miscellaneous goods	4.78	1.5	1.7	2.5	2.8	1.8	2.1	3.4	1.7	2.3
Transport	9.09	1.4	0.7	-0.1	-0.6	-0.5	-0.1	0.7	0.7	0.4
Miscellaneous services	16.15	1.0	1.9	1.7	2.2	2.2	1.3	1.0	*	0.2

**Table 23 : Rates of change in implicit price deflators of GDP
and its main expenditure components**

(%)

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Private consumption expenditure	1.1	-5.0	-3.3	-1.1	-3.6	-2.5	-0.3
Government consumption expenditure	2.9	-0.2	-1.8	1.1	-0.5	-2.6	-2.9
Gross domestic fixed capital formation	-6.9	0.5	-1.0	-6.6	-9.9	-9.4	2.6
Total exports of goods	-3.0	-3.4	-0.3	-2.6	-2.9	-1.8	0.9
Imports of goods	-4.8	-2.4	0.7	-3.5	-4.2	-0.9	2.9
Exports of services	-4.8	-3.2	0.5	-4.3	-2.4	-3.1	0.5
Imports of services	-4.8	-1.3	1.7	-1.1	0.3	2.7	4.1
Gross Domestic Product	0.8	-4.5	-3.6	-1.9	-3.5	-6.2	-3.5
Total final demand	-2.4	-3.3	-1.1	-2.7	-3.6	-2.8	0.6
Domestic demand	-1.2	-3.1	-2.6	-2.3	-4.9	-4.2	0.1

Notes : (#) Figures are subject to revision later on as more data become available.

(*) Change within $\pm 0.05\%$.

**Table 23 : Rates of change in implicit price deflators of GDP
and its main expenditure components (Cont'd)**

	(%)								
	<u>2005</u>	<u>2006[#]</u>	<u>2007[#]</u>	<u>2007</u>				<u>Average annual rate of change:</u>	
				<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>10 years</u> <u>1997 to</u> <u>2007[#]</u>	<u>5 years</u> <u>2002 to</u> <u>2007[#]</u>
Private consumption expenditure	1.8	1.3	3.8	1.9	2.3	3.9	6.6	-0.8	0.8
Government consumption expenditure	-1.4	1.2	3.3	1.3	4.0	3.9	4.0	-0.1	-0.5
Gross domestic fixed capital formation	1.0	4.2	-4.3	-4.3	-4.9	-6.7	-1.5	-3.1	-1.3
Total exports of goods	0.6	0.3	2.1	2.3	1.7	1.7	2.5	-1.0	0.4
Imports of goods	1.9	2.1	1.6	2.1	1.2	0.9	2.3	-0.7	1.5
Exports of services	3.3	3.6	2.7	2.9	2.2	2.6	3.1	-0.8	1.4
Imports of services	1.0	0.8	2.9	2.3	2.5	2.9	3.7	0.6	2.3
Gross Domestic Product	-0.1	-0.3	2.8	1.2	1.8	3.3	4.7	-2.0	-1.5
Total final demand	1.2	1.2	2.1	1.8	1.5	1.8	3.2	-1.1	0.4
Domestic demand	1.2	1.9	1.9	0.3	1.0	1.5	4.3	-1.3	0.2

