

CHAPTER 3 : THE EXTERNAL SECTOR

Summary

- *Hong Kong's external sector continued to fare strongly in 2010, having started the recovery since mid-2009, thanks to the robust economic performance of Asian economies, particularly the Mainland. The sustained recovery in the US and Europe, albeit at a rather modest pace given their weak fundamentals, also helped. Yet external trade lost some steam towards the end of the year. This was more evident in respect of the merchandise trade flows than service trade flows.*
- *Total exports of goods sustained rapid growth during most of 2010, against the low base of comparison created by the collapse of world trade in early 2009. The sharp rebound in 2010 as a whole had more than offset the record annual decline in 2009. The Asian markets continued to outperform the US and EU markets, mirroring the divergent pattern of global economic recovery across regions. However, the growth momentum of merchandise exports slowed towards the end of the year, against the backdrop of a higher base of comparison and the slower growth of some overseas economies in the latter part of 2010.*
- *Exports of services stayed vibrant throughout 2010, having displayed much resilience to the impact of the global financial crisis during 2009. Strong growth momentum was maintained in all four quarters. Exports of travel services surged noticeably amid thriving inbound tourism. Exports of trade-related and transportation services also grew strongly, in tandem with the marked revival in trade flows. The expansion of exports of financial and business services was likewise sizable, supported by intensive fund-raising activities and robust business conditions.*
- *Hong Kong saw further progress in deepening economic linkages with the Mainland and other markets in 2010. The Supplement VII to the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) signed in May 2010 extended the coverage of service areas to 44. Hong Kong's renminbi (RMB) business was brought to new heights with the significant expansion of cross-border trade settlement, deposits, bond issuance and the introduction of financial products. Hong Kong also further enhanced ties with other markets in 2010 through various initiatives over the year.*

Visible trade

Total exports of goods

3.1 Hong Kong's merchandise exports maintained robust growth during most of 2010, having reverted to year-on-year growth in late 2009, capitalising on the sustained robust performance of Asian economies as well as the gradual recovery in the advanced economies. In 2010, *total exports of goods* (comprising re-exports and domestic exports) grew strongly by 18.1% in real terms⁽¹⁾. Such hefty growth partly reflected the depth of the trough in 2009, when there was a record decline of 12.0%. On a year-on-year comparison, export growth in the first three quarters of 2010 was particularly sizable, at 23.4%, 19.7% and 23.2% respectively in real terms. It then tapered to 7.9% in the fourth quarter, amid the effect of a higher base of comparison and slower pace of expansion in some export markets. On a seasonally adjusted quarter-to-quarter comparison, total exports of goods leaped by 6.7% in real terms in the first quarter of 2010, and grew further by 3.6% and 1.9% respectively in the second and third quarters, before showing a 4.1% decline in the fourth quarter.

3.2 The global economy continued to recover over the course of 2010. However, growth pace remained diverse across regions. In the US and Europe, economic recovery proceeded at a moderate pace, partly supported by the earlier stimulus measures and restocking cycle, yet their labour markets were slow to improve. Housing market in the US remained in a depressed state, and the sovereign debt issue in Europe lingered on. On the other hand, many Asian economies, particularly the Mainland, displayed robust growth throughout 2010. The strong regional demand in Asia, coupled with the gradual revival in the advanced economies, propelled trade flows in the Asian region, rendering a staunch support to Hong Kong's export performance in 2010.

3.3 *Re-exports*⁽²⁾, the mainstay of overall merchandise exports and accounting for 97.7% of total export value, rose substantially by 18.1% in real terms in 2010, more than offsetting the decline of 11.3% in 2009. *Domestic exports*, which constitute the remaining share of total exports, likewise bounced back by 15.5% in 2010, having contracted by 34.6% in the previous year.

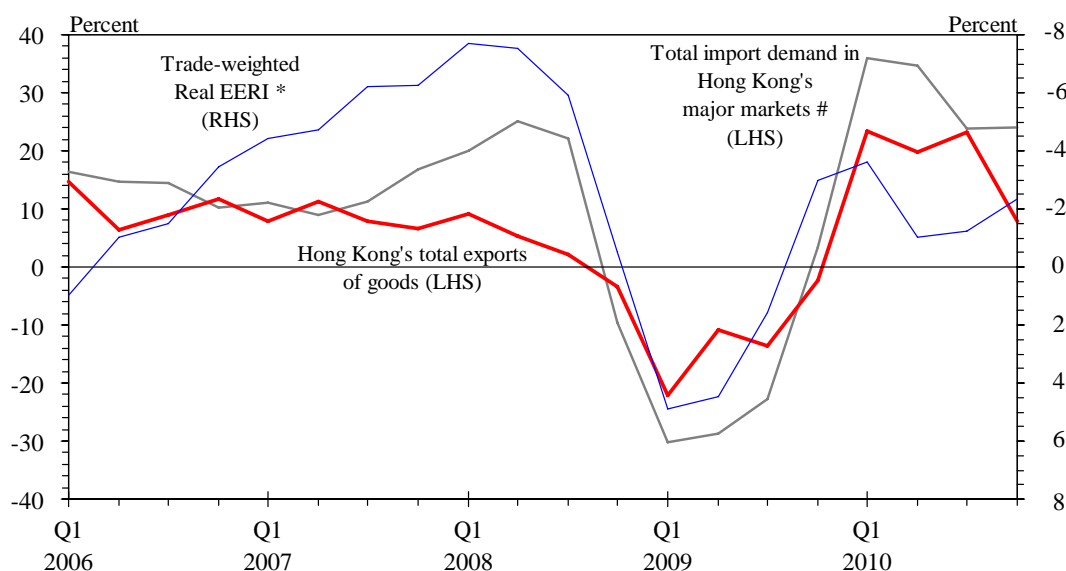
**Table 3.1 : Total exports of goods, re-exports and domestic exports
(year-on-year rate of change (%))**

	<u>Total exports of goods</u>			<u>Re-exports</u>			<u>Domestic exports</u>		
	In value terms	In real terms	Change in prices	In value terms	In real terms	Change in prices	In value terms	In real terms	Change in prices
2009 Annual	-12.6	-12.0	1.1	-11.8	-11.3	1.2	-36.4	-34.6	-0.2
Q1	-21.9	-22.2 (-14.6)	2.5	-21.1	-21.4 (-14.4)	2.5	-44.3	-43.3 (-20.4)	2.5
Q2	-12.9	-10.8 (7.4)	0.8	-12.0	-9.9 (7.7)	0.8	-39.6	-37.0 (-2.3)	*
Q3	-14.3	-13.6 (-2.1)	0.2	-13.5	-12.9 (-2.0)	0.3	-38.7	-35.1 (-5.1)	-2.2
Q4	-2.0	-2.3 (9.7)	0.8	-1.4	-1.8 (9.8)	0.9	-21.2	-21.6 (8.2)	-1.2
2010 Annual	22.8	18.1	4.7	22.8	18.1	4.6	20.4	15.5	5.5
Q1	26.0	23.4 (6.7)	2.8	26.1	23.5 (6.5)	2.8	23.1	20.2 (17.0)	3.2
Q2	24.3	19.7 (3.6)	4.0	24.4	19.7 (3.7)	3.9	22.4	17.0 (-3.3)	6.1
Q3	27.8	23.2 (1.9)	5.2	27.9	23.4 (2.0)	5.2	20.2	14.9 (-4.4)	5.7
Q4	14.4	7.9 (-4.1)	6.5	14.3	7.9 (-4.3)	6.5	16.7	11.1 (3.2)	6.7

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

(*) Change of less than 0.05%.

**Diagram 3.1 : Merchandise exports fared strongly in 2010
(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 2010 is based on statistics for October and November 2010.

Diagram 3.2 : Both re-exports and domestic exports expanded sizably in 2010

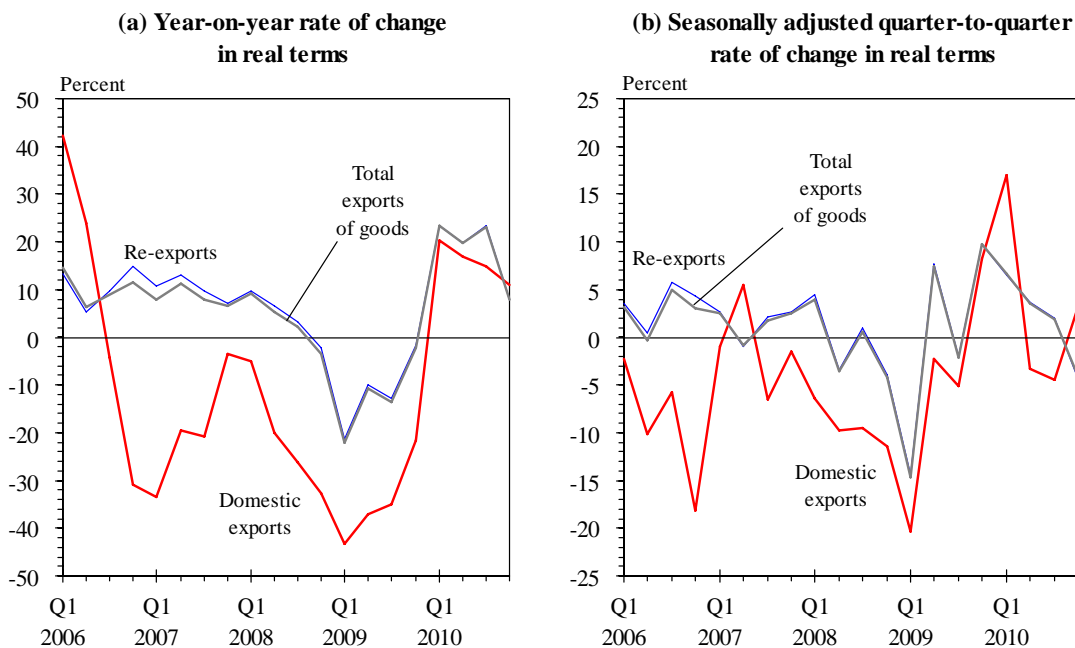
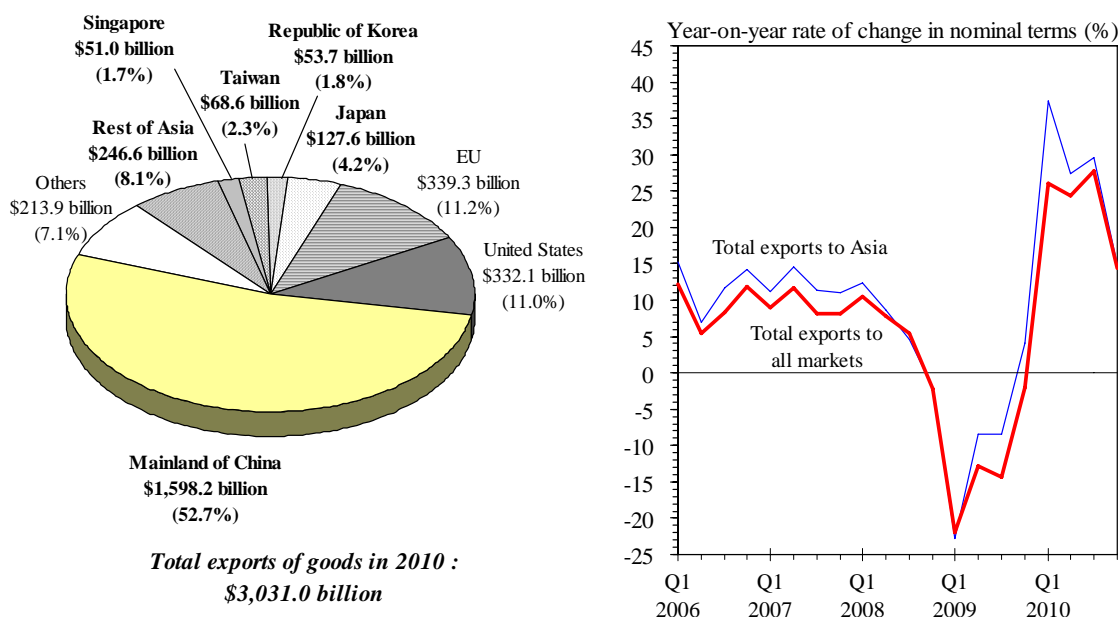


Diagram 3.3 : The Asian markets continued to outperform the US and EU markets



**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>
2009	Annual	-6.6	-20.5	-21.2	-11.8	-14.3	-3.8	-25.0
	Q1	-20.2	-24.6	-22.1	-17.8	-31.9	-27.4	-37.0
	Q2	-1.3	-21.6	-22.6	-19.6	-20.8	-9.6	-27.9
	Q3	-7.9	-22.5	-25.6	-8.2	-11.5	-0.8	-20.2
	Q4	1.5	-13.4	-14.4	-2.2	11.2	21.6	-13.1
2010	Annual	20.0	14.5	6.6	15.5	21.1	23.0	18.1
	Q1	32.1	6.7	-0.6	15.1	37.9	59.8	16.9
	Q2	18.8	19.9	10.4	26.2	24.9	28.1	18.6
	Q3	26.3	19.7	15.8	15.4	13.1	17.6	22.2
	Q4	7.0	10.4	1.0	7.4	13.4	2.8	14.7

3.4 The performance of Hong Kong's merchandise exports to the major markets mirrored the two-speed recovery of the global economy. The Mainland and other Asian markets, which account for around 70% of Hong Kong's total exports of goods, remained the key growth driver, registering a significant increase of around 20% in real terms in 2010. Exports to the Mainland, Singapore, Taiwan, South Korea and Japan all recorded double-digit growth for the year as a whole, in the region of 15-23%. Exports of raw materials and capital goods to many Asian markets picked up strongly amid brisk production activities and robust investment demand in the region. Exports of consumer goods to the Asian markets also displayed strength, rebounding strongly in 2010, more than offsetting the decline in 2009. However, in the final months of the year, as the stimulus from the restocking cycle in the global economy wore off gradually and as growth in demand in the US and Europe remained modest, industrial production and export activities across Asia saw some moderation, resulting in some tapering of growth in Hong Kong's exports to these Asian markets.

3.5 Exports to the US and Europe also rebounded notably during most of 2010 from the collapse in 2009. However, exports to these markets still fell short of the pre-crisis peaks in 2008. In particular, exports of consumer goods, a dominant proportion of exports to these markets, had yet to make up for the decline in 2009 despite some recovery in 2010. Consumer sentiments remained rather cautious in these advanced economies amid the weak labour market conditions. In particular, the EU market still lagged behind others, as the sovereign debt problem lingered on. Exports to this market decelerated sharply to only a small year-on-year growth in the fourth quarter.

Diagram 3.4 : Exports to the Mainland stayed robust in 2010

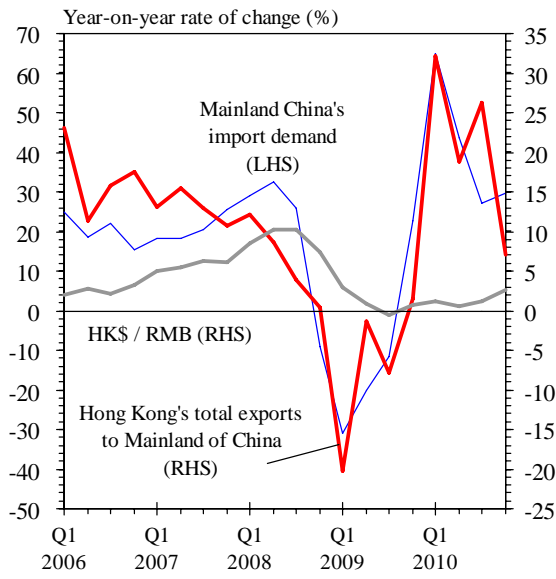


Diagram 3.5 : Exports to the EU still lagged behind other major markets

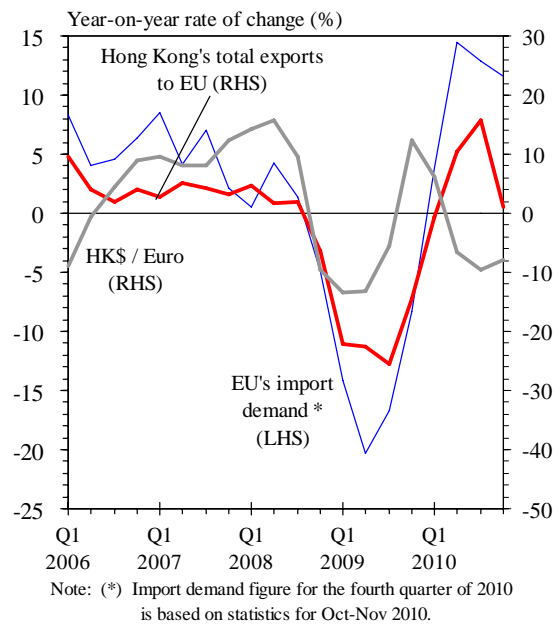


Diagram 3.6 : Exports to the US recovered notably

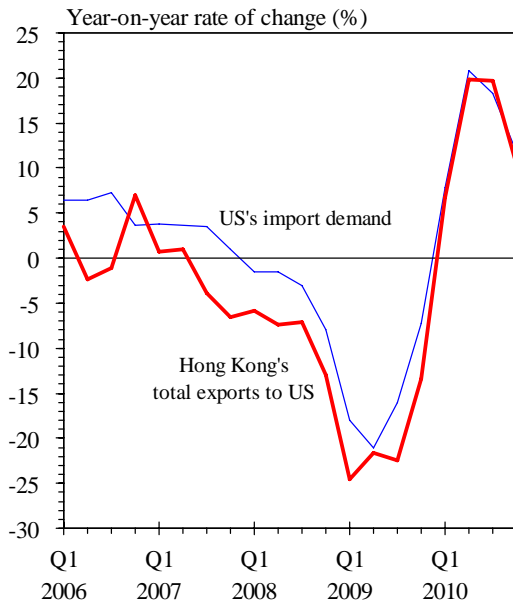


Diagram 3.7 : Exports to Japan showed slower growth towards year-end

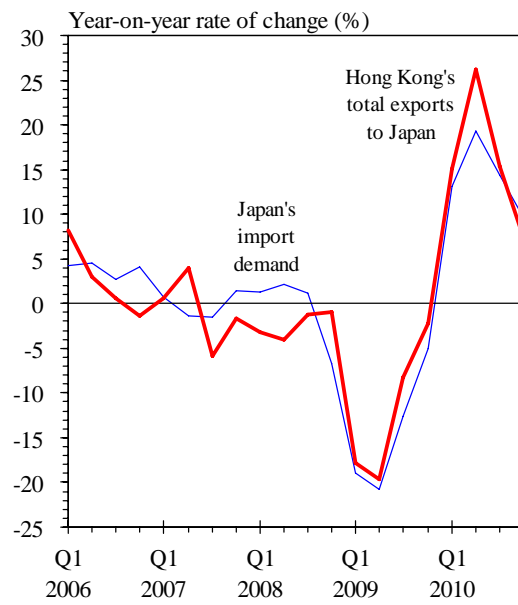


Diagram 3.8 : Exports to Singapore registered double-digit growth in 2010

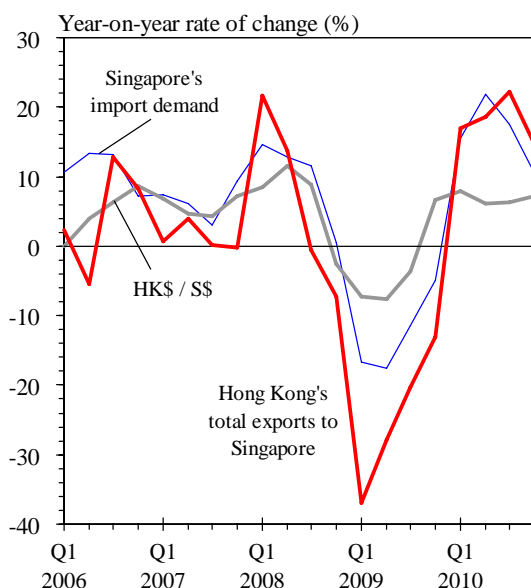
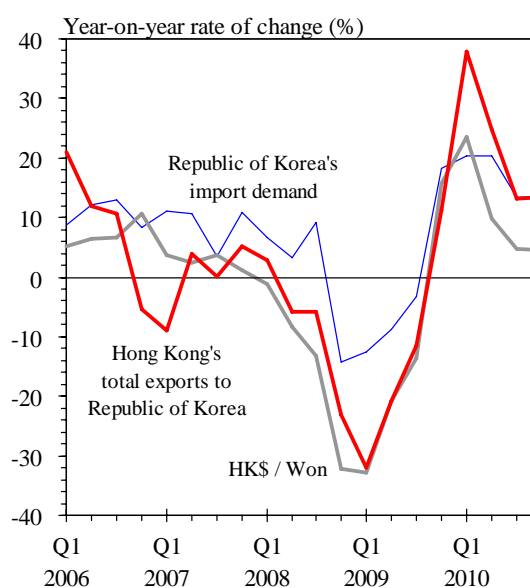


Diagram 3.9 : So did exports to the Republic of Korea



Imports of goods

3.6 *Imports of goods* expanded markedly by 18.6% in real terms in 2010 after a 9.4% decline in 2009, in tandem with the strong rebound in re-export trade and the strengthening of local demand. *Retained imports*, referring to imports for domestic uses, went up by 19.7% in real terms for 2010 as a whole, following the 3.8% decline in 2009. There was a strong year-on-year expansion of 42.1% in the first half of the year, followed by a further increase of 3.8% in the second half of the year as the effect of a much higher base of comparison set in. Analysed by end-use categories, retained imports of raw materials and semi-manufactures saw the fastest growth in 2010, at 31.3% in real terms, albeit reversing to decline in the second half of 2010. Retained imports of consumer goods also performed strongly, up 22.5% along with sanguine consumer sentiments. Retained imports of capital goods surged by 15.5%, in tandem with robust investment and economic activities. Retained imports of fuels and foodstuffs also grew notably by 13.9% and 11.6% respectively in real terms.

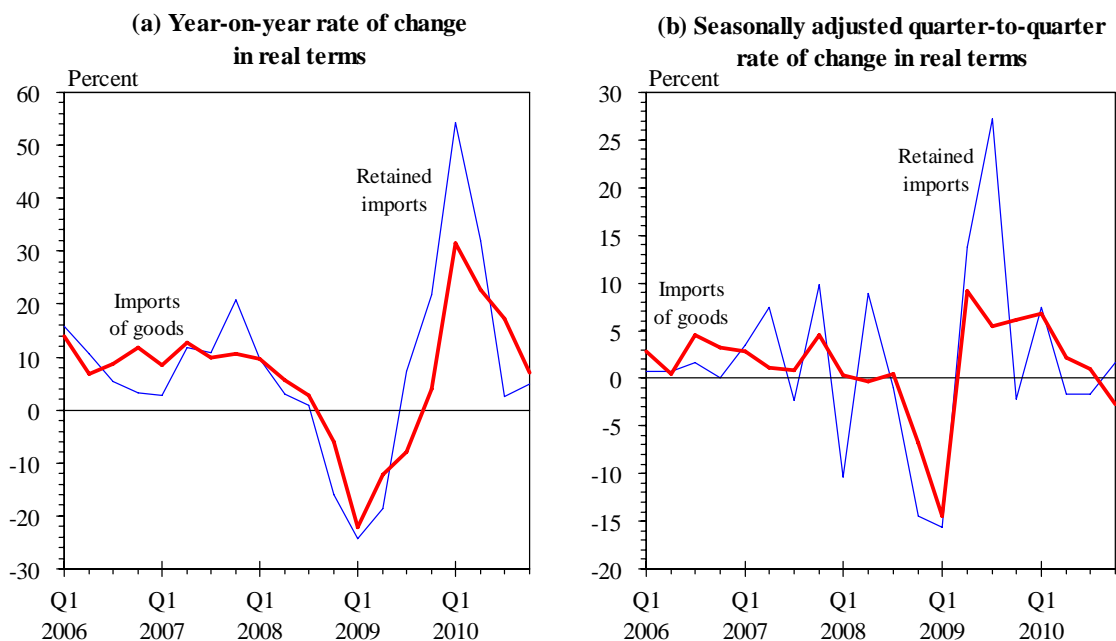
**Table 3.3 : Imports of goods and retained imports
(year-on-year rate of change (%))**

		<u>Imports of goods</u>			<u>Retained imports^(a)</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>
2009	Annual	-11.0	-9.4	-0.1	-10.8	-3.8	-5.8
	Q1	-22.8	-22.2 (-14.4)	1.0	-29.2	-24.2 (-14.6)	-5.8
	Q2	-14.9	-12.3 (9.2)	-0.8	-24.5	-18.6 (13.8)	-7.4
	Q3	-10.4	-7.9 (5.4)	-1.5	-3.3	7.3 (27.2)	-8.2
	Q4	3.4	4.0 (6.1)	0.6	16.3	21.8 (-2.2)	-2.1
2010	Annual	25.0	18.6	6.4	31.3	19.7	11.6
	Q1	34.3	31.4 (6.8)	3.6	60.5	54.2 (7.4)	6.1
	Q2	29.9	22.8 (2.2)	6.6	47.2	32.0 (-1.6)	14.8
	Q3	24.1	17.3 (1.0)	7.2	13.7	2.5 (-1.6)	13.3
	Q4	15.1	7.0 (-2.7)	8.2	17.2	5.0 (1.7)	13.0

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 3.10 : Both imports and retained imports grew robustly in 2010



**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>
2009	Annual	-8.8	7.0	-4.4	-9.7	23.2
	Q1	-30.7	-3.4	-8.1	-69.5	30.8
	Q2	-22.4	6.3	-13.4	-47.4	17.4
	Q3	0.1	11.1	-3.7	41.1	24.1
	Q4	20.8	13.4	7.6	68.2	21.1
2010	Annual	22.5	11.6	15.5	31.3	13.9
	Q1	48.7	28.6	21.2	344.4	-0.2
	Q2	32.9	8.5	24.2	70.8	42.6
	Q3	7.2	2.8	7.2	-18.1	14.6
	Q4	12.6	8.6	12.1	-13.9	1.4

Invisible trade

Exports of services

3.7 *Exports of services* sustained strong growth throughout 2010, leaping by 15.0% in real terms for the year as a whole, following the 0.3% growth in 2009. Despite the higher base of comparison, exports of services still grew at a rapid pace in the fourth quarter of 2010. Among the major service components, exports of travel services showed the strongest performance, thanks to the sizable influx of visitors from the regional as well as long-haul markets. Exports of trade-related services, reflecting mainly offshore trade, grew sharply in 2010, benefiting from the improved trading environment for Asia. Exports of transportation services likewise surged along with the expansion of trade flows and flourishing passenger flows. Exports of financial and business services were also strong, on the back of the intensive fund-raising activities in the financial market and the brisk expansion of business activities.

Diagram 3.11 : Trade-related and transportation services accounted for nearly 60% of service exports, reflecting Hong Kong's position as a trading hub

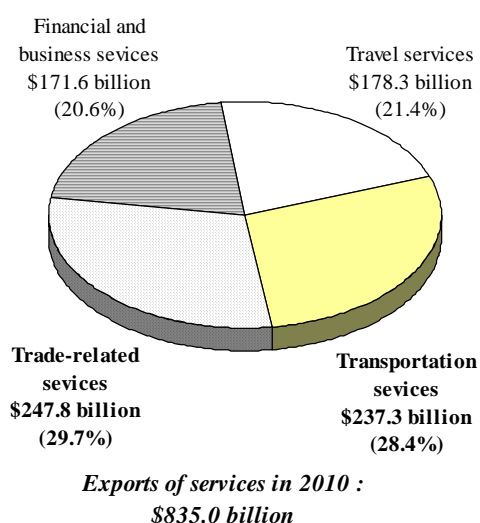


Diagram 3.12 : Exports of services sustained strong growth throughout 2010

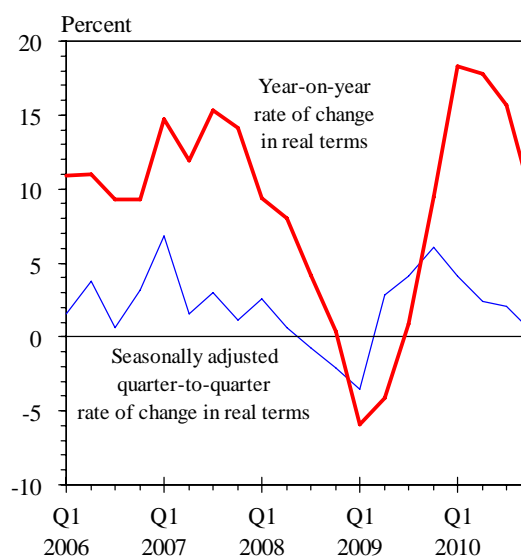


Table 3.5 : Exports of services by major service group (year-on-year rate of change in real terms (%))

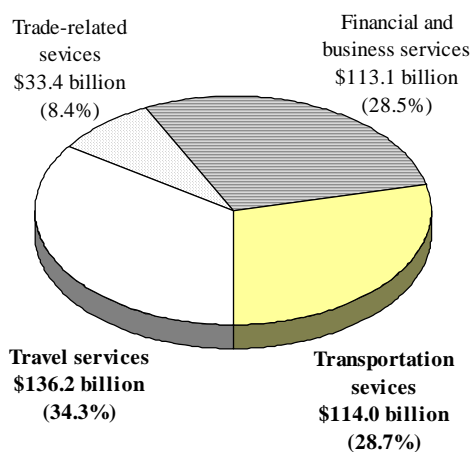
		<i>Of which :</i>				
		Exports of services	Trade-related services ^(a)	Transportation services	Travel services ^(b)	Financial and business services
2009	Annual	0.3	-5.2	-1.8	7.9	5.1
	Q1	-5.9 (-3.5)	-13.0	-10.4	15.3	-5.5
	Q2	-4.1 (2.8)	-10.1	-3.3	-1.7	-0.7
	Q3	0.9 (4.1)	-6.9	1.5	1.4	11.2
	Q4	9.5 (6.1)	5.8	4.8	14.9	17.1
2010	Annual	15.0	14.3	9.1	29.2	12.6
	Q1	18.3 (4.1)	20.7	15.6	19.5	18.2
	Q2	17.8 (2.4)	18.0	11.0	39.2	12.6
	Q3	15.7 (2.1)	14.1	8.6	43.1	8.3
	Q4	9.4 (0.4)	8.2	2.3	19.7	11.2

Notes : (a) Comprising mainly offshore trade.
 (b) Comprising mainly inbound tourism receipts.
 () Seasonally adjusted quarter-to-quarter rate of change.

Imports of services

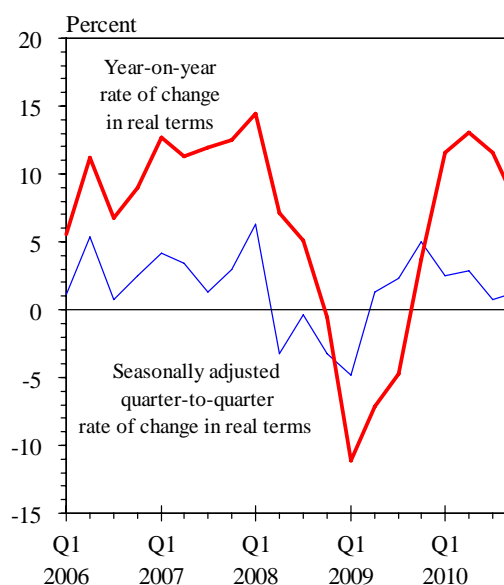
3.8 *Imports of services* were likewise robust, up 10.9% in real terms in 2010, in contrast to the 4.9% contraction in 2009. Imports of travel services grew solidly further along with improving economic conditions. Imports of trade-related services and transportation services both thrived on the strong rebound in offshore trade amid vibrant intra-regional trade flows. Imports of financial and business services also picked up markedly to a double-digit increase in 2010.

Diagram 3.13 : Travel and transportation services featured more prominently in imports of services



Imports of services in 2010 :
\$396.6 billion

Diagram 3.14 : Imports of services were likewise robust



**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>Financial and business services</u>	
2009	Annual	-4.9	0.1	-19.9	0.7	6.9	
	Q1	-11.1	(-4.8)	-7.2	-25.1	-7.7	-0.7
	Q2	-7.1	(1.3)	2.7	-21.0	-4.7	-0.3
	Q3	-4.7	(2.3)	-1.3	-18.8	-1.1	10.0
	Q4	3.7	(5.0)	7.2	-14.4	12.3	18.6
2010	Annual	10.9	7.3	12.5	15.8	12.6	
	Q1	11.6	(2.5)	5.2	13.0	22.3	15.9
	Q2	13.1	(2.9)	7.3	16.5	19.6	15.8
	Q3	11.6	(0.7)	11.6	11.9	15.7	10.0
	Q4	7.8	(1.3)	5.2	8.4	9.8	9.6

Notes : (+) Comprising mainly outbound travel spending.

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

Visible and invisible trade balance

3.9 With strong import intake amid the robust upturn in the Hong Kong economy, the visible trade deficit widened in 2010. Nevertheless, this was more than offset by the gain in invisible trade surplus, thanks to vibrant service exports across a broad front. As a result, the combined visible and invisible trade balance in 2010 recorded a surplus of \$104.6 billion, equivalent to 2.8% of the total value of imports of goods and services. This compared with the corresponding figures of \$121.3 billion and 4.0% in 2009. The favourable trade balance continues to underline Hong Kong's strong external competitiveness.

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

		<u>Total exports</u>		<u>Imports</u>		<u>Trade balance</u>			As % of imports
		<u>Goods</u>	<u>Services</u>	<u>Goods</u>	<u>Services</u>	<u>Goods</u>	<u>Services</u>	<u>Combined</u>	
2009	Annual	2,495	670	2,703	341	-208	330	121	4.0
	Q1	512	154	547	77	-35	77	43	6.8
	Q2	619	144	658	78	-39	65	26	3.5
	Q3	657	177	723	90	-66	86	21	2.5
	Q4	706	196	775	96	-68	100	32	3.7
2010	Annual	3,061	835	3,395	397	-334	438	105	2.8
	Q1	640	191	728	92	-88	99	11	1.4
	Q2	774	186	871	93	-97	94	-4	-0.4
	Q3	838	221	898	104	-60	117	57	5.7
	Q4	809	237	898	108	-89	129	40	4.0

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

Other developments

3.10 Hong Kong saw further notable progress in deepening the economic linkages with the Mainland during 2010. Specifically for the services sector, access of local professional services to the Mainland market was further broadened through the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) platform. Supplement VII to CEPA was signed on 27 May 2010 and the relevant services liberalisation measures were implemented on 1 January 2011. The new supplement provides for 35 market liberalisation and trade and investment facilitation measures in 19 sectors, bringing the total number of service sectors under CEPA to 44.

3.11 Hong Kong also made a big leap forward in its role as Mainland's offshore renminbi (RMB) business centre. Of particular note was the expansion of the cross-border RMB trade settlement scheme, first in June 2010, whereby the coverage was extended from trade transactions between five Mainland cities and the ASEAN economies to all trade transactions of 20 Mainland provinces and cities⁽³⁾ with the rest of the world, and then in December 2010, with the number of eligible Mainland enterprises that can settle merchandise exports in RMB increasing substantially from 365 to 67 359. The amount of trade settlement in RMB conducted in Hong Kong showed phenomenal growth towards the latter part of the year, with the amount of cross-border settlement rising markedly from a monthly average of RMB4 billion in the first half of 2010 to that of RMB26 billion in the third quarter, and further to RMB88 billion in the fourth quarter.

3.12 Economic co-operation between Hong Kong and Taiwan also developed further. After the implementation of the “Three Direct Links” across the Taiwan Strait, trade between the Mainland and Taiwan expanded markedly by 37.7% in 2010. Yet Hong Kong was able to benefit from such a development, with Hong Kong’s re-exports involving trade across the Strait surging by 31.0% in 2010. The Economic Cooperation Framework Agreement (ECFA) signed by Mainland and Taiwan on 29 June 2010 further promoted regional trade flows. In addition, to facilitate multi-faceted and multi-level exchanges with Taiwan, the Hong Kong-Taiwan Economic & Cultural Co-operation Promotion Council and the Hong Kong-Taiwan Business Co-operation Committee were established in April 2010. Hong Kong will continue to strengthen its exchanges with Taiwan to take advantage of the expansion in economic activity in the region arising from these developments.

3.13 The Government had also been active in promoting linkages with new and emerging markets in 2010. The Hong Kong-New Zealand Closer Economic Partnership Agreement was signed in March 2010, the first of its kind for Hong Kong with a foreign economy. The Agreement came into force on 1 January 2011⁽⁴⁾. Exchanges had also been broadened through enhanced contacts with other emerging markets such as Russia, India, the Middle East and South America to encourage more enterprises from these markets to invest in Hong Kong, and to help our enterprises tap the business opportunities in these markets. Indeed, Hong Kong’s total merchandise exports to Russia and India surged by 105% and 42% respectively in 2010 alone, and by about 200% and 240% respectively over the past five years. India has now emerged to become the fifth largest market for Hong Kong’s exports. Hong Kong will continue to position itself to leverage on its role as a platform to reach Guangdong, the rest of the Mainland and the Asia-Pacific region.

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) The cities and provinces are: Beijing, Tianjin, Inner Mongolia, Liaoning, Shanghai, Jiangsu, Zhejiang, Fujian, Shandong, Hubei, Guangdong, Guangxi, Hainan, Chongqing, Sichuan, Yunnan, Jilin, Heilongjiang, Xizang and Xinjiang.
- (4) Under the Agreement, New Zealand will phase out over six years its import tariffs on all goods originating in Hong Kong, and more than 90% of New Zealand's tariff lines will become duty free within two years after the agreement has come into force. Hong Kong service providers will also enjoy secured preferential opportunities in the New Zealand market in a variety of service sectors.