

CHAPTER 1 : OVERVIEW OF ECONOMIC PERFORMANCE IN 2013

Summary

- *Hong Kong's overall economic performance improved in 2013, with real GDP expanding moderately by 2.9%, up from 1.5% in 2012, keeping the labour market in a state of full employment. The growth pace was nevertheless slower than the average annual growth of 4.5% over the past decade, as global economic performance remained subpar under the drag of sluggishness of advanced economies and the consequential growth slowdown in emerging markets. Domestic demand and exports of services provided the key driving forces for overall economic growth in 2013. In the fourth quarter, the economy showed further moderate growth, at 3.0% year-on-year.*
- *Total exports of goods, after excluding the notable surge in exports of non-monetary gold, grew only modestly during most of 2013, mainly reflecting the weak demand conditions in Europe, fiscal drag on US economic growth, and slower activity expansion in emerging markets amid concerns about the Federal Reserve's asset purchase tapering. Nevertheless, the advanced markets showed some relative improvements in the second half of the year as the eurozone resumed growth and the US economy gained more traction.*
- *Exports of services attained solid growth in 2013 and provided an important impetus to the economy. Underpinned by vibrant inbound tourism, exports of travel services grew at a double-digit pace and were the standout performer. Exports of financial and other business services also picked up gradually throughout the year amid improved global business sentiment and acceleration in fund-raising activities. Meanwhile, exports of transportation and those of trade-related services remained rather subdued alongside the sluggish regional and international trade flows.*
- *The domestic sector saw steady growth in 2013. Private consumption expenditure grew further, thanks largely to the favourable job and income conditions. Investment rose only moderately, due to relapse in private sector construction activities. Yet infrastructure construction works remained hectic, while investment in machinery and equipment attained another year of double-digit growth.*
- *The labour market was tight, with job vacancies rising to record highs and total employment sustaining notable growth. The seasonally adjusted unemployment rate edged down to 3.2% in the fourth quarter, indicating further tightening in employment situation. Against this background, wages and earnings registered further gains.*

- *Local stock prices exhibited considerable fluctuations during the year, and ended the year slightly higher than a year ago. After going lower in the mid-year on jitters about less monetary accommodation in the US and the ensuing volatility in the emerging markets, the stock market regained lost ground in the second half of the year as the advanced economies improved and the Mainland economy displayed its resilience. The local property market turned quiet, with the increases in flat prices slowing and activities down, after the Government's introduction of further demand-side management measures in late February.*
- *Consumer price inflation was largely contained during 2013, as imported inflation went lower and helped offset the domestic price pressures. For 2013 as a whole, underlying inflation averaged 4.0%, marking the second year of easing from 5.3% in 2011 and 4.7% in 2012.*

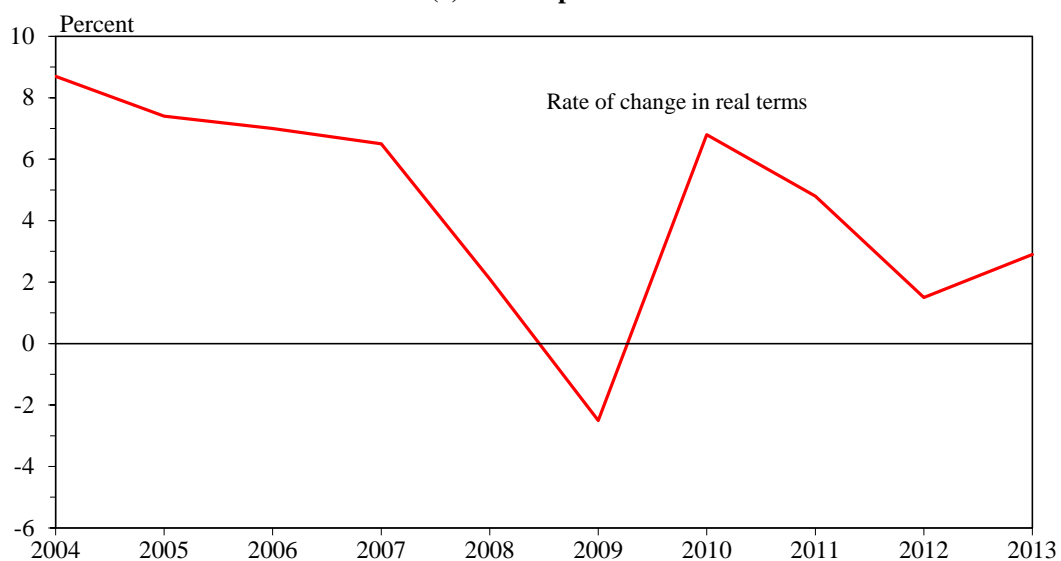
Overall situation

1.1 The Hong Kong economy attained a moderate growth in 2013 amid a still challenging external environment. The growth pace, while representing a relative improvement over that in 2012, was still slower than the trend in the past ten years. Merchandise exports were held back by the subpar global economic conditions given the weak momentum in the EU market, the fiscal retrenchment in the US, and widespread growth slowdown in emerging markets amid the threat from the Federal Reserve's talks about asset purchase tapering. In 2013, the Mainland and some other Asian markets provided the main support to Hong Kong's export growth. Global economic sentiment improved towards the end of the year, along with the improvements in the advanced economies. However, this had yet to translate into a more visible growth in international trade flows. Exports of services performed relatively better, thanks mainly to the vibrant inbound tourism and expansion of financial activity. Amid favourable labour market conditions and further support from infrastructure works, domestic demand expanded solidly and played an important stabilizing role. Underlying inflation held largely stable in 2013, with incipient signs of easing towards the end of the year.

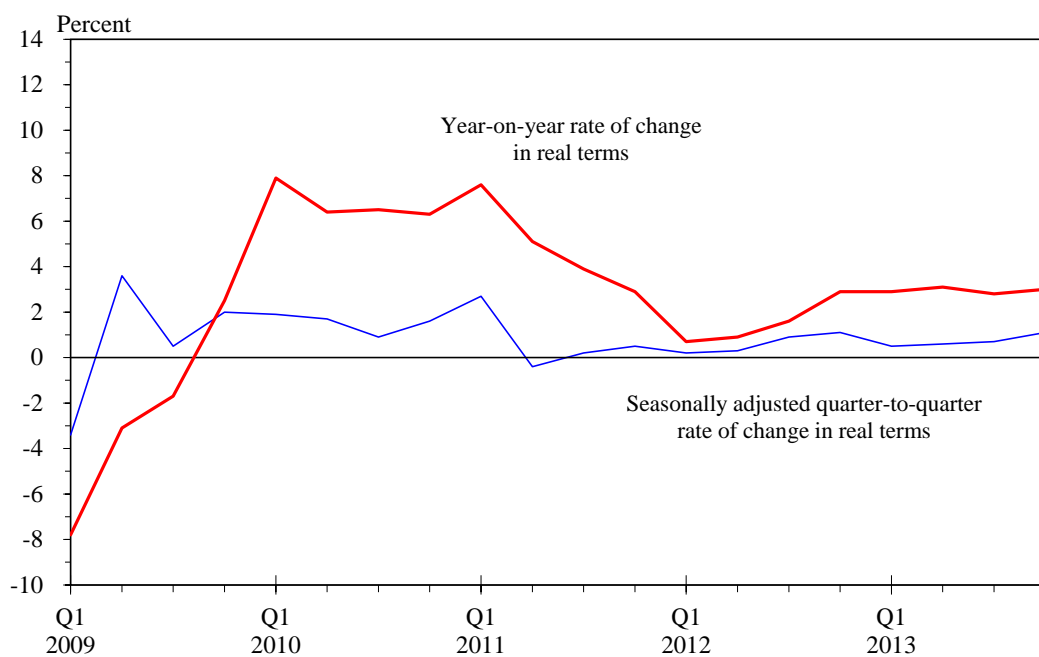
1.2 For 2013 as a whole, *Gross Domestic Product* (GDP)⁽¹⁾ grew by 2.9% in real terms, improved from the 1.5% growth in 2012, but still below the annual average growth of 4.5% in the past decade. Real GDP growth hovered at around 3% throughout the four quarters, at 2.9%, 3.1%, 2.8% and 3.0% respectively. On a seasonally adjusted quarter-to-quarter comparison⁽²⁾, real GDP growth picked up successively during the year, at 0.5%, 0.6%, 0.7% and 1.1% respectively in the first, second, third and fourth quarters.

Diagram 1.1 : The Hong Kong economy picked up to moderate growth in 2013

(a) Annual profile



(b) Quarterly profile



The external sector

1.3 *Total exports of goods* compiled under the GDP accounting framework grew by 6.7% in real terms in 2013, after the slight growth of 1.8% in 2012. Excluding the substantial increase in exports of non-monetary gold, exports saw only moderate growth. The performance of the advanced markets remained disappointing, despite some relative improvement in the second half of the year. The US market stayed subdued, only showing moderated decline in the second half of 2013. By comparison, the EU market fared better and returned to modest growth in the second half of the year after nine quarters of contraction alongside the stabilisation in eurozone activity. Meanwhile, exports to the major Asian markets were mixed. Exports to Japan fell notably amid a weaker yen, while those to the Mainland and India grew solidly during most of 2013. In terms of the quarterly profile, the year-on-year growth of merchandise exports after excluding non-monetary gold in real terms decelerated from 4.0% in the first quarter to 2.4% and 2.0% respectively in the second and third quarters, before picking up slightly to 3.1% in the fourth quarter. On a seasonally adjusted quarter-to-quarter comparison, merchandise exports declined in the first and second quarters, yet resumed growth in the third and fourth quarters.

1.4 *Exports of services* continued to perform better than those of goods, rising by 5.8% in real terms for 2013 as a whole, notably improved from the 2.2% increase in 2012. Thanks to buoyant inbound tourism, exports of travel services grew rapidly, thereby rendering the key impetus to overall exports of services. Exports of financial and other business services also gathered pace gradually during the year, as cross-border financial and fund-raising activities accelerated. Bound by the sluggishness in merchandise trade flows, exports of trade-related and transportation services remained rather subdued in 2013.

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

	<u>2012[#]</u>	<u>2013[±]</u>	<u>2012</u>				<u>2013</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	4.1	4.2	6.5 (1.1)	3.5 (0.4)	2.7 (1.4)	3.7 (1.1)	6.5 (3.1)	4.6 (-1.1)	2.4 (-0.4)	3.2 (1.7)
Government consumption expenditure	3.6	2.7	3.1 (1.3)	4.2 (0.7)	4.0 (0.8)	3.3 (0.3)	2.2 (0.3)	3.1 (1.5)	2.3 (0.2)	3.2 (1.1)
Gross domestic fixed capital formation	6.8	3.3	9.9	3.9	5.3	8.5	-3.3	7.6	2.8	5.3
<i>of which :</i>										
Building and construction	7.2	-1.2	9.5	8.6	2.0	8.9	-2.4	-1.0	3.2	-4.1
Machinery, equipment and intellectual property products	10.2	10.5	20.4	5.7	9.4	8.1	-4.3	19.4	7.3	17.2
Total exports of goods	1.8	6.7	-4.7 (0.8)	0.3 (-0.3)	4.6 (3.2)	6.7 (3.3)	8.8 (1.5)	6.2 (-1.4)	6.2 (3.2)	5.8 (2.1)
Imports of goods	3.0	7.6	-1.8 (3.0)	1.2 (-0.8)	4.7 (2.3)	7.6 (3.7)	9.6 (3.5)	7.6 (-1.8)	6.8 (1.9)	6.5 (2.5)
Exports of services	2.2	5.8	2.8 (0.6)	2.6 (0.6)	0.1 (-0.7)	3.3 (2.9)	5.1 (2.1)	8.0 (3.2)	5.5 (-2.6)	4.9 (2.3)
Imports of services	1.9	1.5	4.5 (1.9)	2.5 (-0.7)	0.1 (-1.9)	0.9 (1.4)	0.5 (1.5)	-1.0 (-1.7)	2.7 (1.7)	3.7 (2.3)
Gross Domestic Product	1.5	2.9	0.7 (0.2)	0.9 (0.3)	1.6 (0.9)	2.9 (1.1)	2.9 (0.5)	3.1 (0.6)	2.8 (0.7)	3.0 (1.1)
<i>Change in the main price indicators (%)</i>										
GDP deflator	3.7	1.2	3.6 (1.2)	2.9 (0.9)	4.0 (1.0)	4.1 (0.4)	1.2 (-1.0)	0.4 (0.2)	1.5 (1.7)	1.6 (0.6)
Composite CPI										
Headline	4.1	4.3	5.2 (1.2)	4.2 (0.8)	3.1 (-2.0)	3.8 (3.7)	3.7 (1.1)	4.0 (1.3)	5.3 (-0.8)	4.3 (2.7)
Underlying[^]	4.7	4.0	5.9 (1.2)	5.1 (0.9)	4.0 (0.5)	3.8 (1.1)	3.8 (1.1)	3.9 (1.1)	4.3 (0.8)	4.0 (1.0)
Change in nominal GDP (%)	5.3	4.2	4.4	3.8	5.7	7.1	4.2	3.5	4.4	4.6

Notes : Figures are subject to revision later on as more data become available. Seasonally adjusted quarter-to-quarter rate of change is not applicable to gross domestic fixed capital formation, as no clear seasonal pattern is found for the category due to the presence of considerable short term fluctuations. Figures of private consumption expenditure, exports of goods, and imports and exports of services were revised back to 2009 as a result of a technical revision exercise conducted by the Census and Statistics Department in mid-2013. For details, please see Note (3) to this chapter.

(#) Revised figures.

(+) Preliminary figures.

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

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

The domestic sector

1.5 The domestic sector held firm in 2013 and provided buffer against the external headwinds. Thanks to the favourable labour market conditions, *private consumption expenditure* (PCE) grew by 4.2% in real terms in 2013, similar to the 4.1% growth in the previous year. On a seasonally adjusted quarter-to-quarter comparison, PCE expanded strongly in the first quarter, then fell back in the second and third quarters, before picking up in the fourth quarter. *Government consumption expenditure* increased steadily further by 2.7% in real terms in 2013, following the 3.6% growth in 2012.

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

		<i>Of which :</i>							
		Total consumer spending in the domestic market ^(a)	Food	Durables	Non-durables	Services	Residents' expenditure abroad	Visitor spending	Private consumption expenditure ^(b)
2012	Annual	5.1	3.6	13.2	7.9	2.5	4.6	10.1	4.1
	H1	5.6	2.4	20.3	9.0	2.1	6.4	10.1	5.0
	H2	4.5	4.8	7.7	6.8	2.9	2.9	10.0	3.3
	Q1	6.7	1.0	25.5	11.6	2.5	6.9	8.0	6.5
	Q2	4.6	3.7	15.1	6.6	1.7	6.0	12.5	3.5
	Q3	3.4	5.4	4.1	5.2	2.1	4.7	7.4	2.7
	Q4	5.5	4.2	10.7	8.1	3.6	1.0	12.4	3.7
2013	Annual	6.5	4.6	7.0	14.9	3.2	4.5	17.7	4.2
	H1	8.8	3.9	14.5	18.7	4.4	2.5	23.2	5.5
	H2	4.4	5.2	0.5	11.4	2.0	6.4	13.1	2.8
	Q1	8.7	4.2	28.0	11.4	4.1	5.5	18.5	6.5
	Q2	8.8	3.7	*	26.1	4.8	-0.3	28.1	4.6
	Q3	4.6	5.2	-0.6	12.6	2.2	4.7	15.6	2.4
	Q4	4.3	5.3	1.4	10.5	1.7	8.2	10.8	3.2

Notes : (a) Consumer spending in the domestic market comprises both local consumer and visitor spending. Figures of private consumption expenditure, exports of goods, and imports and exports of services were revised back to 2009 as a result of a technical revision exercise conducted by the Census and Statistics Department in mid-2013. For details, please see Note (3) to this chapter.

(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.

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

Diagram 1.2 : Private consumption expenditure maintained moderate growth in 2013

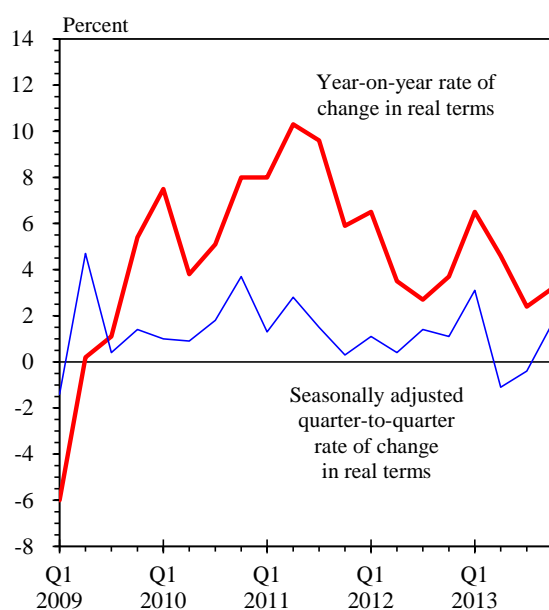
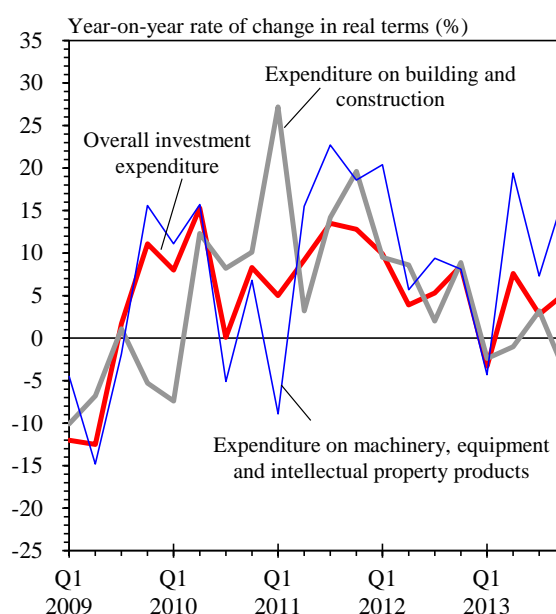


Diagram 1.3 : Investment spending expanded moderately in 2013



1.6 Overall investment spending in terms of *gross domestic fixed capital formation* posted a modest growth of 3.3% in real terms in 2013, moderating from the growth of 10.2% and 6.8% respectively in 2011 and 2012. Machinery and equipment acquisition grew notably by 10.5% in 2013, largely in line with the positive business sentiment indicated by the results of the Quarterly Business Tendency Survey on large enterprises, even though the diffusion indices on small and medium-sized enterprises (SMEs) revealed a slightly more cautious picture (see **Box 1.1** for details of the consultation on SMEs). In 2013, public sector construction works grew solidly further, on the back of continued hectic infrastructure works. Yet, private sector building activity fell back, thereby leading to a slight decline of 1.2% in overall building and construction expenditure in real terms.

Box 1.1

Diffusion indices on small and medium-sized enterprises (an update)

To gain a better understanding of the current situation of business receipts, employment and credit access for small and medium-sized enterprises (SMEs)⁽¹⁾, an ad-hoc consultation exercise has been conducted by the Census and Statistics Department on behalf of the Economic Analysis and Business Facilitation Unit since late November 2008 on a sample panel of around 500 SMEs to solicit their feedback. This note provides a further update of the results reported in **Box 1.1** in the *Third Quarter Economic Report 2013*.

From June 2011 onwards, the industry coverage and questionnaire design for the exercise have been modified. Specifically, three sectors (viz. travel agents, financing institutions, and insurance agents and brokers) are dropped from the exercise, while questions on access to credit have been modified to gauge SMEs' views as to whether the current and expected credit access situation are "easy", "fair" or "tight", rather than in respect of a comparison with the normal times. The sample size of the panel has consequently been reduced to around 400.

A set of diffusion indices is compiled to indicate the general directions of change in the respondents' views on business receipts and employment versus the preceding month. While the findings should be interpreted with considerable caution given the coverage and nature of the consultation exercise, they can serve as a rough indicator to enable high frequency monitoring of SMEs' situation.

Business receipts of the SMEs consulted, as depicted by the set of diffusion indices, showed that the overall situation remained weak in January 2014, with the readings for all the selected sectors below the boom-bust threshold of 50 (**Table 1**). Among all the selected sectors, the diffusion indices for retail trade and restaurants performed relatively better, in line with continued solid growth of retail sales. The reading for the real estate sector was still the lowest, reflecting a quiet property market under the influence of the Fed's tapering and the sustained effects of the Government's demand-side management measures. As regards the external segment, the diffusion indices for the import/export trades and logistics sectors receded, conceivably indicating the cautiousness among SMEs in these sectors in the face of renewed gyrations in the financial markets at the start of this year. As to the employment situation, the feedback from SMEs indicated broadly stable development in recent months (**Table 2**).

Specifically for SMEs in the import and export sector, their views on new export orders were sought separately to help gauge the likely export performance in the near term. The diffusion index on new export orders inched lower in January 2014, but was still close to the boom-bust threshold of 50, pointing to broadly stable external demand conditions. However, uncertainties remain, particularly those arising from the US monetary policy and its possible negative impacts on the growth of emerging market economies.

(1) Manufacturing enterprises with fewer than 100 employees and non-manufacturing enterprises with fewer than 50 employees are regarded as SMEs in Hong Kong.

Box 1.1 (Cont'd)

The proportion of SMEs reporting tight credit access, while rising back to 1.5% in January 2014 from 0.6% in the preceding month, was still at a relatively low level, thanks to the generally accommodative monetary conditions and the Government's continued efforts to support SMEs through various loan guarantee schemes. Nevertheless, whether this rising trend would continue in the coming months still warrants monitoring.

Table 1 : Diffusion indices[^] on business receipts

	<u>2013</u>												<u>2014</u>
	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul</u>	<u>Aug</u>	<u>Sep</u>	<u>Oct</u>	<u>Nov</u>	<u>Dec</u>	<u>Jan</u>
<i>Local segments</i>													
Restaurants	49.2	48.4	48.3	45.8	46.7	45.8	48.2	48.2	47.4	47.4	48.2	49.1	48.1
Real estate	51.5	39.7	39.7	38.2	42.6	44.1	44.1	35.3	35.3	41.2	36.8	44.1	42.4
Retail trade	46.3	47.7	48.1	47.6	47.6	47.1	49.0	50.0	49.0	47.5	48.0	49.0	47.4
Wholesale trade	47.2	47.2	47.2	44.4	50.0	47.1	41.2	44.1	47.1	50.0	44.1	47.1	44.7
Business services	50.0	53.0	47.0	43.9	48.5	48.5	45.5	43.9	45.5	50.0	48.5	53.0	47.0
<i>External segments</i>													
Import/export trade	50.0	49.0	51.0	49.0	50.0	50.0	48.1	47.6	48.5	49.0	49.5	49.0	47.9
Logistics	50.0	44.7	47.4	47.4	44.7	50.0	47.4	44.7	44.7	44.7	52.8	50.0	47.2
All the above sectors*	48.9	48.2	48.6	47.0	48.4	48.3	47.3	46.8	47.3	48.1	48.0	49.0	47.0

Notes : (^) The diffusion index is computed by adding the percentage of SMEs reporting "up" to one half of the percentage of SMEs reporting "same". A diffusion index reading above 50 indicates that the business condition is generally favourable, whereas an index below 50 indicates otherwise. Respondents were requested to exclude seasonal effects in reporting their views.

(*) Weighted average using total number of SMEs in individual sectors as weights.

Table 2 : Diffusion indices on employment situation

	<u>2013</u>												<u>2014</u>
	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul</u>	<u>Aug</u>	<u>Sep</u>	<u>Oct</u>	<u>Nov</u>	<u>Dec</u>	<u>Jan</u>
<i>Local segments</i>													
Restaurants	49.2	49.2	49.2	49.2	50.0	48.3	50.0	50.0	49.1	49.1	49.1	48.2	49.1
Real estate	50.0	50.0	50.0	50.0	50.0	48.5	50.0	45.6	48.5	47.1	47.1	47.1	50.0
Retail trade	50.5	50.0	50.0	50.0	50.0	50.0	50.0	50.0	49.5	50.0	50.0	50.0	49.6
Wholesale trade	50.0	50.0	50.0	50.0	50.0	50.0	50.0	47.1	50.0	50.0	50.0	47.1	50.0
Business services	50.0	54.5	53.0	51.5	50.0	50.0	48.5	51.5	48.5	50.0	51.5	50.0	50.0
<i>External segments</i>													
Import/export trade	49.1	50.0	50.5	50.0	50.5	51.0	49.0	49.5	49.5	50.0	51.0	50.0	50.4
Logistics	50.0	50.0	50.0	50.0	50.0	47.4	47.4	50.0	47.4	47.4	50.0	50.0	50.0
All the above sectors*	49.7	50.4	50.5	50.1	50.2	50.1	49.3	49.5	49.3	49.7	50.3	49.5	50.0

Note : (*) Weighted average using total number of SMEs in individual sectors as weights.

Table 3 : Diffusion index on current new export orders

	<u>2013</u>												<u>2014</u>
	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul</u>	<u>Aug</u>	<u>Sep</u>	<u>Oct</u>	<u>Nov</u>	<u>Dec</u>	<u>Jan</u>
Import/export trade	49.1	50.0	50.5	49.0	49.5	49.5	48.5	48.5	48.1	49.5	50.5	49.5	49.2

Table 4 : Percentage of SMEs reporting tight current access to credit

	<u>2013</u>												<u>2014</u>
	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul</u>	<u>Aug</u>	<u>Sep</u>	<u>Oct</u>	<u>Nov</u>	<u>Dec</u>	<u>Jan</u>
All selected sectors*	1.3	1.2	0.7	0.9	0.6	0.6	0.6	0.7	0.7	0.7	0.4	0.6	1.5

Note : (*) Weighted average using total number of SMEs in individual sectors as weights.

The labour sector

1.7 The labour market was in a state of full employment in 2013. Labour demand remained firm, thanks to the largely resilient domestic sector and the vibrant inbound tourism. Total employment attained a notable growth of 2.3% in 2013, while job vacancies increased further to hit new highs during the year. The *seasonally adjusted unemployment rate* edged down to 3.2% in the fourth quarter, with the *underemployment rate* also down to 1.4%. In tandem with the tight labour market conditions, wages and earnings rose further across many sectors during the year, with more notable increases in the lowest decile groups, thanks in part to the demand-supply conditions in the lower-skilled segment and an additional boost from the upward adjustment of the Statutory Minimum Wage rate in May.

The asset markets

1.8 The *local stock market* remained volatile in 2013 and finished the year slightly higher. Spooked by the Fed's asset purchase tapering discussion and the attendant stock and foreign exchange market gyrations in emerging economies, the local stock market came under sharp sell-off pressure during May and June. The Hang Seng Index (HSI) hit a low of 19 814 on 24 June 2013. The stock market recovered ground in the ensuing months upon indications by the Fed on its continued accommodative stance, a faster Mainland's growth in the third quarter, and improved economic sentiment in Europe and the US. The HSI closed the year at 23 306, up 2.9% from end-2012. The average daily turnover also rebounded modestly to \$62.6 billion in 2013. Fund-raising activity likewise picked up in 2013, particularly in the fourth quarter. For the year as a whole, total IPO funds raised amounted to \$169.0 billion in 2013, up from \$90.0 billion in 2012. Hong Kong ranked as the world's second largest IPO centre in 2013.

1.9 *Residential property market* turned quiet after the Government rolled out further demand-side management measures in late February, compounded by the Fed's signal in the mid-year to reduce asset purchases. Transaction volume fell visibly by 38% in 2013. Residential property prices rose only at an average pace of 0.2% per month since March, in stark contrast to the 2.7% per month in the first two months of the year. Nevertheless, overall flat prices in December 2013 were still 8% higher than a year earlier and 42% above the 1997 peak, while the affordability ratio hovered at around 54% in the fourth quarter of 2013, well above the long-term average of 48% over 1993-2012. Likewise, flat rentals rose at a more moderate pace, cumulating to a 3% gain for 2013 as a whole, down from 11% in 2012. As for

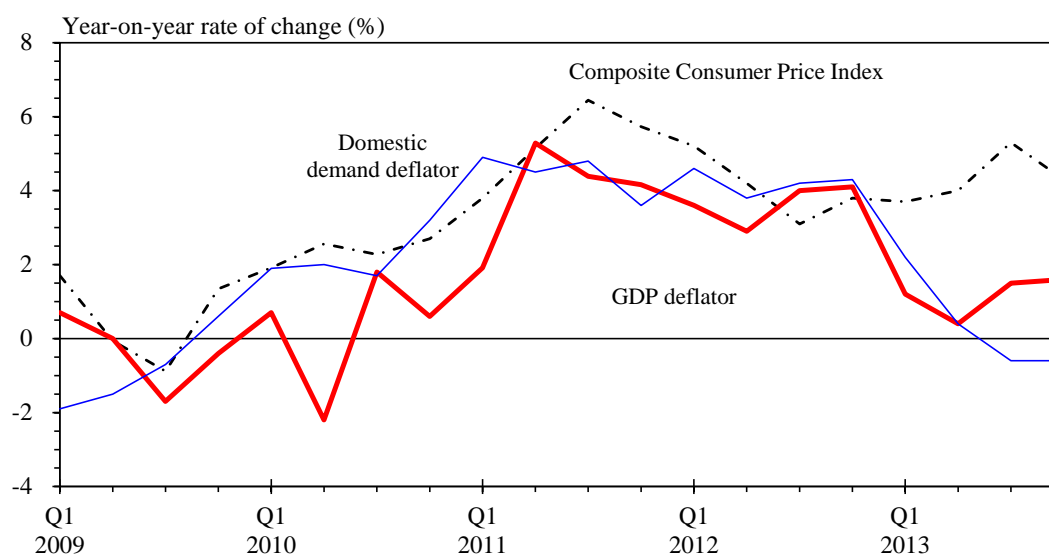
non-residential property market, rentals for shops went up by 6%, visibly slower than the 13% increase during 2012. Office rentals rose by 7% during 2013, also slower than the increase of 8% in the preceding year.

Inflation

1.10 Consumer price inflation was largely stable in 2013. Netting out the effects of the Government's one-off relief measures, *underlying consumer price inflation* actually retreated to 4.0% in 2013, down from 5.3% and 4.7% respectively in 2011 and 2012. The moderation in the underlying rate mainly reflected the benefits from subdued external price pressure while some notable upward price pressures domestically also tended to stabilise in the latter part of 2013. In particular, increases in the private housing rentals component began to ease at the end of 2013 as the feed-through of milder increases in fresh-letting private residential rentals earlier kicked in. As further signs of easing price pressure, the average monthly rates of change in the underlying Consumer Price Index on a seasonally adjusted basis retreated to 0.2% in the fourth quarter, down from 0.3% in the first half in 2013 and 0.4% in the third quarter. Wage growth in 2013 held at a pace somewhat slower than that in 2012. *Headline consumer price inflation*, which is influenced by the Government's relief measures, edged up to 4.3% in 2013 from 4.1% in 2012, reflecting in part the spike in July 2013 caused by a lower base of comparison upon the Government's payment of public housing rentals the same month in the previous year, and is by no means an indication of a rising underlying inflation trend.

1.11 The *GDP deflator* increased by 1.2% in 2013, likewise slower than the increase in 2012, amid moderated increase in prices for consumption expenditure, and a visible decline in prices for machinery and equipment.

Diagram 1.4 : Consumer price inflation was largely stable in 2013



GDP by major economic sector

1.12 The services sector grew moderately in the first three quarters of 2013, in line with the overall economic performance. Net output in real terms grew by 2.7%, 3.8% and 2.5% respectively in the first three quarters of 2013 over a year earlier. Most sectors saw some improvements when compared with the weak 2012 outcomes. Net output of import and export trade showed slightly faster growth in the first two quarters before slowing somewhat in the third quarter, reflecting the still unsteady external trading environment, while that of financing and insurance accelerated markedly in the first three quarters as the global investment climate stabilised. Professional and business services also grew at a faster pace in the second and third quarters amid improved business sentiment. Information and communications, and accommodation and food services both expanded moderately in the first three quarters. Real estate activity, which mainly reflects the net output of private sector developers and property agency activity, contracted in all three quarters amid a quiet property market, while the net output of the construction sector was underpinned by an acceleration of infrastructure works and picked up notably in the third quarter. Meanwhile, net output growth in transportation and storage remained subdued over the period while activity in the manufacturing sector stayed weak, in part related to the sluggish trade and production activity.

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

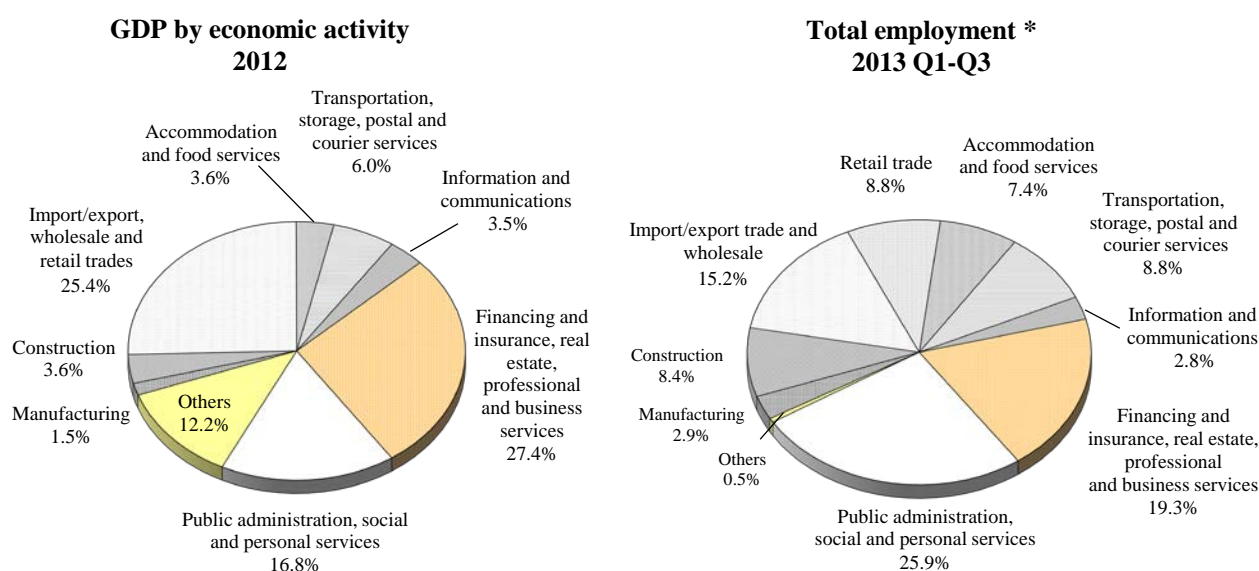
	<u>2012</u>	<u>2013</u>	<u>2012</u>				<u>2013</u>		
		<u>Q1-Q3</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
Manufacturing	-0.8	-0.1	-1.6	-2.9	-0.1	1.3	0.5	0.3	-0.9
Construction	8.3	3.1	10.8	7.2	1.2	13.1	-1.4	2.6	8.8
Services ^(b)	1.8	3.0	1.4	0.9	2.0	2.7	2.7	3.8	2.5
Import/export, wholesale and retail trades	1.9	3.8	-0.1	0.6	2.1	4.1	5.1	4.8	1.9
Import and export trade	0.6	2.2	-2.4	-0.9	1.5	3.4	3.3	2.7	0.9
Wholesale and retail trades	7.3	10.5	10.2	7.2	4.5	7.6	12.4	13.1	6.4
Accommodation ^(c) and food services	1.8	4.0	-0.8	0.9	2.8	4.1	4.3	4.3	3.4
Transportation, storage, postal and courier services	0.9	1.5	3.0	-1.7	0.4	1.8	-0.6	3.0	2.4
Transportation and storage	0.7	1.0	3.0	-1.9	0.2	1.2	-0.9	2.8	1.2
Postal and courier services	6.4	14.1	3.2	1.6	7.4	12.5	7.7	6.5	27.9
Information and communications	2.8	4.6	0.7	1.4	4.1	4.5	6.5	2.6	4.6
Financing and insurance	0.8	6.0	2.2	-0.9	1.0	1.1	3.7	7.9	6.4
Real estate, professional and business services	3.1	-0.2	3.4	4.5	3.2	1.7	-0.3	-0.3	-0.2
Real estate	3.9	-4.2	3.3	5.8	4.3	2.5	-2.5	-5.9	-4.3
Professional and business services	2.3	3.8	3.1	3.1	2.2	1.1	2.2	5.4	3.8
Public administration, social and personal services	2.1	2.7	2.1	2.2	2.2	1.8	2.1	3.8	2.3

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 services sectors include ownership of premises as well, which is analytically a service activity.
- (c) Accommodation services cover hotels, guesthouses, boarding houses and other establishments providing short term accommodation.

1.13 The services sector is the mainstay of the Hong Kong economy, generating 93.0% of GDP in 2012 and providing 88.2% of the total employment in the first three quarters of 2013. Buttressed by our institutional advantages and a highly effective and professional workforce, the services sector has met the challenges of globalisation, and its focus has increasingly shifted towards the high value-added and knowledge-based activities. With the aid of the competitive service sector, Hong Kong is well-positioned to benefit from the nation's strategy of rebalancing towards a more consumer-based, service-led economy. The Hong Kong economy will keep up its competitiveness as an international financial centre and a regional business hub, by consolidating the strength of the traditional pillar industries, developing new industries with growth potential, and upgrading its infrastructure and human capital. On the latter, it is worth noting that the proportion of the local workforce with tertiary education attainment increased steadily from 31.4% in 2008 to 34.9% in 2013.

Diagram 1.5 : The services sector is the key driver of the economy



Note : (*) Figures refer to the Composite Employment Estimates, which are compiled based on results of the General Household Survey and the Quarterly Survey of Employment and Vacancies. Figures for 2013 are averages for the first three quarters of the year.

Other economic developments

1.14 The challenges confronting Hong Kong in 2013 were notable. The damages caused by the financial tsunami and the euro debt crisis on the world economies continued to constrain our export performance, while the bubble risks in the property market remained prominent given the additional monetary easing in the advanced economies. In anticipation of a difficult environment, the Government included a package of relief measures amounting to some \$33 billion in the 2013-14 Budget to help the people and enterprises to counter the headwinds.

1.15 To forestall the build-up of bubble risks in the property market, the Government introduced further demand-side management measures and a sixth round of macro-prudential measures in late February, while continuing its efforts to increase land supply. Along with the prospect of diminishing US monetary support, the property market cooled off visibly in 2013.

1.16 Hong Kong's institutional strength continues to be well recognised internationally, ranking as the world's freest economy by the Heritage Foundation for the 20th year in a row and topping the league in World Economic Forum's (WEF) Financial Development Index for two consecutive years. Despite these recognitions, the Government will strive to lift our competitiveness further and achieve long-term economic growth, by consolidating our existing strength, fostering economic integration with the Mainland, and strengthening our ties with other parts of the world.

1.17 To reinforce our strength in financial services, several positive initiatives were taken in 2013. In July, the Inland Revenue and Stamp Duty Legislation (Alternative Bond Schemes) (Amendment) Ordinance 2013 came into operation, which would help establish a platform for the development of Islamic finance and facilitated the issuance of sukuk products. In the same month, the Hong Kong Monetary Authority introduced two measures to enhance the provision of RMB liquidity to Authorized Institutions participating in RMB business in Hong Kong to foster the further development of Hong Kong as an offshore RMB business hub.

1.18 As an important part of our development strategy, Hong Kong continues to deepen its economic integration with the Mainland to take full advantage of the "Mainland factor". To this end, Supplement X to the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) was signed in August, providing for a total of 73 services liberalisation and trade and investment facilitation measures. Along with the measures in the

previous rounds, the CEPA and its supplements cover a wide range of service sectors such as financial, tourism, construction, legal, medical and accounting services and offer preferential treatments for Hong Kong service suppliers, in tapping the vast potential of the Mainland market. In addition, further cooperation agreements with the Pan-Pearl River Delta region and Guangdong were signed in September, paving the way for deeper economic collaboration with other provinces in the Mainland. Given the Central Government's support and our distinctive institutional advantages, Hong Kong is also poised to benefit from the coming wave of deepening economic reforms and opening-up unveiled by the Third Plenary Session of the 18th Communist Party of China Central Committee in November.

1.19 Beyond the Mainland, Hong Kong also constantly explores ways to forge closer trade relations with other economies, especially with emerging markets. In late February, Hong Kong and Thailand signed a cooperation agreement to promote collaborations on merchandise and service trade, investment, and other areas. Meanwhile, facilitative tax agreements were also signed with other trading partners to promote trade and investment flows. The Bali Package concluded at the Ninth Ministerial Conference of the World Trade Organisation in Bali in December represents a significant breakthrough, as the agreement has been a concrete step forward after the Doha Round talks launched in 2001, which may help restore momentum in future multilateral trade negotiations. Amongst the various elements of the Bali Package, the new Agreement on Trade Facilitation should benefit Hong Kong as an international trading hub and related industries, notably trading and logistics.

1.20 To brace for the ageing population and the Government's other long-term financial commitments, the Working Group on Long-Term Fiscal Planning was established in June to formulate a more comprehensive public finances plan. The Working Group is charged with assessing long-term public expenditure needs and changes in government revenue, and proposing feasible measures with reference to overseas experience.

1.21 The Chief Executive presented the 2014 Policy Address on 15 January 2014, formulating strategic directions and measures to unleash Hong Kong's growth potential and support the needy while nurturing the next generation to prepare for the transition ahead.

- On the economic front, the Government will continue its effort to consolidate our existing competitive advantages, deepen economic links with the Mainland and overseas markets in every aspect, and foster diversity and robust growth in our industries. The Government will,

among other things, follow up on recommendations from the Financial Services Development Council to strengthen our position as an international financial centre, increase the number of Economic and Trade Offices in the Mainland and the rest of Asia to enhance our liaison work and tap new markets, and commence formal negotiations for a Hong Kong-ASEAN Free Trade Agreement. By attaining sustained economic growth, the Government will be on a stronger foundation to meet other pressing needs of the community such as housing, education, poverty, an aging society and environmental protection.

- To take full advantage of the Hong Kong-Zhuhai-Macao Bridge when it is completed, a Lantau Development Advisory Committee will be formed to find ways to further develop the eastern waters off Lantau Island and neighbouring areas with a view to transform the areas into an East Lantau Metropolis.
- On housing issues, the Government has accepted the recommendation of the Steering Committee of the Long Term Housing Strategy to increase land and housing supply, with the new housing target set at a total of 470 000 units in the coming ten years, of which 60% coming from the public sector.
- The Government is committed to foster young people by devoting considerable resources to formal education, strengthening vocational education and encouraging whole-person development outside the classroom settings, through which our next generation are better prepared to contribute to the society in future. On poverty alleviation, the Government will roll out new measures to encourage young people and adults in low-income families to become self-reliant through employment while providing a reasonable and sustainable social security and welfare system to help those who cannot provide for themselves.

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.
- (3) In mid-2013, Census and Statistics Department conducted a technical revision exercise to review the estimation method of cross-boundary movements of goods and services in the GDP compilation framework. As a result of the exercise, estimates of private consumption expenditure, exports of goods, and imports and exports of services were revised back to 2009. The levels and growth rates pertaining to the entire series of overall GDP were however not affected by this non-routine revision, as the exercise involved only re-classification of consumption expenditure on goods and services between residents and non-residents.