

CHAPTER 1 : OVERVIEW OF ECONOMIC PERFORMANCE

Summary

- *The Hong Kong economy continued to expand notably in the third quarter, by 3.6% over a year earlier, following the 4.1% growth in the first half of 2017. This marked the fourth consecutive quarter of above-trend economic expansion. External demand stayed vibrant, supported by the broadly benign global economic conditions. Domestic demand attained further solid growth, mainly underpinned by firm private consumption.*
- *Benefitting from a broad-based global economic upturn, Hong Kong's total exports of goods maintained visible growth in the third quarter, with those to the Asian markets staying as the major propelling force. Meanwhile, exports of services picked up in the third quarter, thanks to vibrant regional trade and cargo flows and the recovery in inbound tourism.*
- *Domestic demand stayed firm in the third quarter. Private consumption expenditure held up particularly well, as local consumer sentiment was well underpinned by the favourable job and income conditions and to a certain extent by stronger wealth effects. Overall investment expenditure, on the other hand, recorded a modest decline, as machinery and equipment acquisition, a volatile component, fell. Nevertheless, building and construction works accelerated to show solid growth. Results of recent surveys also continued to suggest that business sentiment remained positive.*
- *The labour market remained in a state of full employment. In the third quarter, the seasonally adjusted unemployment rate held steady at a low level of 3.1%, and total employment registered further robust growth. Wages and earnings generally sustained gains in real terms, with those of lower-paid workers continuing to register appreciable growth.*
- *The local stock market was largely on the rise in the third quarter, alongside the rallies in major overseas markets. The moderation of the residential property market continued in the third quarter, with visibly lower trading activities and slower increase in prices.*
- *Inflation pressure was largely contained. Underlying consumer price inflation eased in the third quarter, amid subdued import prices and moderate local cost increases. Specifically, labour cost pressures stayed modest when viewed against the sustained expansion of economic output at an above-trend pace, while the feed-through from higher fresh-letting residential rentals into consumer price inflation was only gradual.*

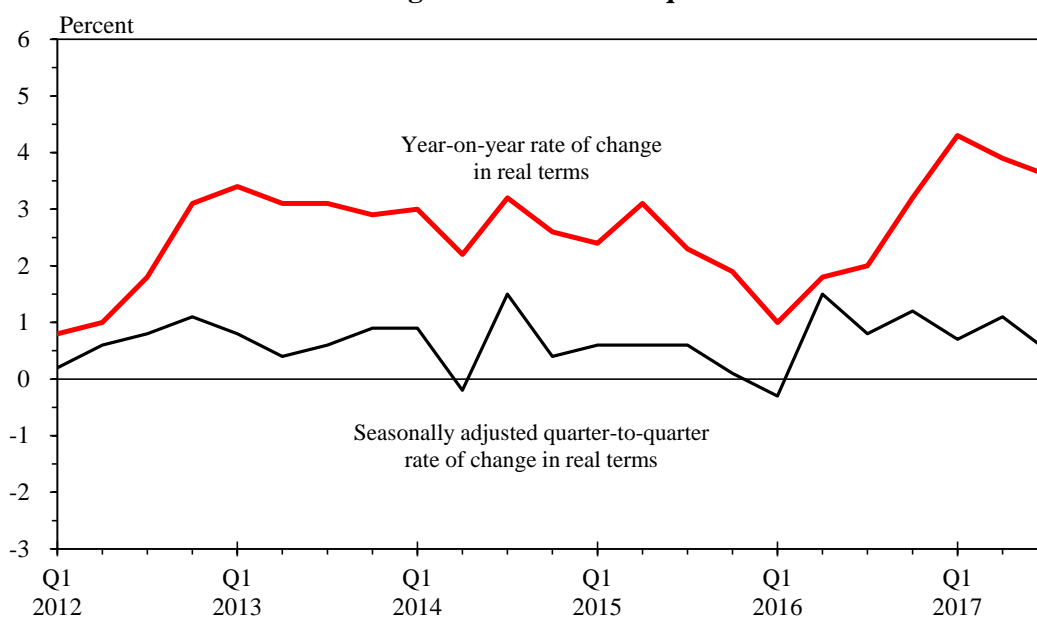
Overall situation

1.1 The Hong Kong economy grew by 3.6% in the third quarter of 2017 over a year earlier, following the 4.1% growth in the first half of the year. The broad-based global economic upturn seen in the first half of the year extended well into the third quarter. This benign external environment continued to render a firm support to Hong Kong's exports of goods and services. Exports of goods to the Asian markets as a whole outperformed those to the other regions. Exports of services picked up in the third quarter, thanks to vibrant regional trade and cargo flows and the recovery in inbound tourism. On the domestic front, private consumption expenditure fared particularly well, underpinned by the favourable job and income conditions, with added support from a somewhat stronger boost from positive wealth effects. Yet, overall investment expenditure reverted to a small decline. In particular, acquisition of machinery and equipment, a volatile component, fell, while costs of ownership transfer went notably lower as property market transactions slowed visibly compared to year-ago levels. Nevertheless, overall building and construction expenditure accelerated to show solid growth, and recent surveys continued to suggest that business sentiment remained positive. The already-moderate underlying consumer price inflation eased further amid modest imported price pressures and contained increases in domestic costs.

1.2 The global economy sustained moderate growth in the third quarter. The US economy continued to expand at a moderate pace in the third quarter, notwithstanding the temporary hurricane-induced disruptions in some southern states. The ongoing economic recovery in the euro area turned more broad-based, underpinned by solid growth in domestic demand and improved economic sentiment. Against these positive developments, the Federal Reserve began trimming its balance sheet in October, and the European Central Bank also announced to reduce its monthly asset purchases starting from early 2018. Meanwhile, the Mainland economy sustained medium-high speed growth, as domestic demand remained robust and exports grew visibly. Economies elsewhere in Asia demonstrated further strength in the third quarter, as trading and manufacturing activities in the region remained vibrant, notwithstanding the escalated geopolitical tensions in Northeast Asia. Acknowledging the progress made in the global economy so far this year, the International Monetary Fund (IMF) revised its global economic forecast for 2017 upwards to 3.6%, representing a pick-up from the 3.2% growth in 2016⁽¹⁾.

1.3 In the third quarter of 2017, *Gross Domestic Product* (GDP)⁽²⁾ grew by 3.6% in real terms over a year earlier, after the notable growth of 3.9% in the preceding quarter (revised from the earlier estimate of 3.8%). This marked the fourth consecutive quarter of economic growth that stayed above the past-ten-year trend rate of 2.9% per annum. On a seasonally adjusted quarter-to-quarter basis⁽³⁾, real GDP grew by 0.5% in the third quarter of 2017, after the strong expansion of 1.1% in the preceding quarter (revised from the earlier estimate of 1.0%).

Diagram 1.1 : The Hong Kong economy continued to show an above-trend growth in the third quarter of 2017



The external sector

1.4 *Total exports of goods* compiled under the GDP accounting framework grew visibly by 5.5% in real terms in the third quarter over a year earlier, the same growth pace as that in the preceding quarter. Among major markets, with reference to external merchandise trade statistics in the third quarter, exports to Asian markets as a whole outperformed those to the other regions, thanks to sustained growth in demand for raw materials, semi-manufactures and capital goods amid vibrant manufacturing activities in the region. Specifically, on a year-on-year comparison in real terms, exports to the Mainland picked up to show notable growth. Exports to Taiwan, Singapore and Japan all attained double-digit growth, and those to India also grew notably. Exports to the EU picked up somewhat to show a moderate growth for the third quarter as a whole, whereas those to the US continued to lag behind by comparison.

1.5 *Exports of services* picked up to grow by 3.7% year-on-year in real terms in the third quarter, from the 2.6% growth in the preceding quarter. Exports of transport services grew notably alongside vibrant trade and cargo flows. Exports of travel services resumed moderate growth after declining for over three years, signifying the recovery of inbound tourism. Exports of financial services picked up amid supportive global financial conditions, while those of business and other services stayed on a modest expansion path.

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

	<u>2015[#]</u>	<u>2016[#]</u>	<u>2016</u>				<u>2017</u>		
			<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3⁺</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>									
Private consumption expenditure	4.8	1.8	1.5 (0.2)	0.4 (0.7)	1.6 (1.1)	3.6 (1.5)	3.9 (0.5)	5.4 (2.1)	6.7 (2.4)
Government consumption expenditure	3.4	3.4	3.2 (0.9)	3.6 (1.0)	3.4 (0.5)	3.4 (0.9)	3.1 (0.6)	3.2 (1.1)	4.1 (1.5)
Gross domestic fixed capital formation	-3.2	-0.3	-8.7	-5.1	7.2	5.6	5.9	7.2	-1.7
Building and construction	2.2	3.9	1.5	2.4	4.3	7.5	8.6	2.4	4.1
Costs of ownership transfer	-8.3	-2.9	-50.9	-19.2	22.5	63.7	77.3	53.2	-12.4
Machinery, equipment and intellectual property products	-7.7	-4.6	-10.8	-10.3	7.6	-4.2	-8.6	4.7	-6.0
Total exports of goods ^{&}	-1.7	1.8	-3.5 (-2.5)	2.4 (3.0)	2.5 (0.7)	5.1 (3.9)	9.3 (1.6)	5.5 (-0.9)	5.5 (0.7)
Imports of goods ^{&}	-2.7	1.1	-5.6 (-3.8)	0.6 (3.6)	3.1 (1.9)	5.6 (4.0)	10.0 (0.3)	6.1 (-0.3)	6.1 (1.9)
Exports of services ^{&}	0.3	-3.2	-5.4 (-1.0)	-6.2 (-0.6)	-2.5 (1.8)	1.2 (1.1)	2.8 (0.6)	2.6 (-1.0)	3.7 (2.8)
Imports of services ^{&}	5.0	2.0	4.1 (1.7)	1.2 (-1.1)	0.8 (-0.2)	2.0 (1.6)	0.9 (0.5)	3.7 (1.8)	1.5 (-2.3)
Gross Domestic Product	2.4	2.0	1.0 (-0.3)	1.8 (1.5)	2.0 (0.8)	3.2 (1.2)	4.3 (0.7)	3.9 (1.1)	3.6 (0.5)
<i>Change in the main price indicators (%)</i>									
GDP deflator	3.6	1.8	2.1 (0.5)	1.7 (0.5)	1.5 (0.2)	1.8 (0.6)	2.1 (0.8)	3.3 (1.6)	3.2 (0.2)
Composite CPI									
Headline	3.0[@]	2.4	2.8 (0.7)	2.6 (-0.6)	3.1 (0.4)	1.2 (0.7)	0.5 (0.1)	2.0 (0.7)	1.8 (0.2)
Underlying[^]	2.5[@]	2.3	2.8 (0.7)	2.3 (0.2)	2.1 (0.5)	2.1 (0.7)	1.4 (0.1)	2.0 (0.7)	1.7 (0.2)
Change in nominal GDP (%)	6.1	3.9	3.2	3.6	3.6	5.0	6.5	7.4	6.9

Notes : Figures are subject to revision later on as more data become available. The seasonally adjusted quarter-to-quarter rate of change is not applicable to gross domestic fixed capital formation, as no clear seasonal pattern is found for this category due to the presence of considerable short term fluctuations.

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

(#) Revised figures.

(+) Preliminary figures.

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

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

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

The domestic sector

1.6 Domestic demand grew solidly in the third quarter. *Private consumption expenditure* held up particularly well, picking up to show year-on-year growth of 6.7% in real terms in the third quarter, following the notable growth of 4.7% in the first half of this year. Local consumer sentiment continued to be well underpinned by favourable job and income conditions, with added support from a somewhat stronger boost from positive wealth effects. Meanwhile, *government consumption expenditure* grew at a slightly faster pace of 4.1% year-on-year in real terms in the third quarter, after growing by 3.2% in the preceding quarter.

**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)
2016 Annual		-0.2	0.9	-13.3	-0.3	1.9	7.1	-8.1	1.8
	H1	-1.7	0.7	-17.9	-2.5	1.1	9.2	-11.0	1.0
	H2	1.2	1.2	-8.8	1.9	2.8	5.1	-5.3	2.7
	Q1	-2.2	-1.8	-17.8	-3.4	1.8	16.6	-13.0	1.5
	Q2	-1.1	2.7	-18.1	-1.5	0.3	2.4	-8.8	0.4
	Q3	*	0.3	-8.1	-2.9	2.2	4.0	-7.4	1.6
	Q4	2.3	2.0	-9.3	6.1	3.3	6.1	-3.3	3.6
2017	H1	4.0	3.3	-0.5	5.7	4.1	4.0	-0.5	4.7
	Q1	3.6	3.3	-1.1	4.5	4.2	-0.2	-0.2	3.9
	Q2	4.3	3.4	0.3	6.8	4.1	8.4	-0.9	5.4
	Q3	6.2	4.6	8.3	9.4	5.1	4.5	2.1	6.7

Notes : (a) Consumer spending in the domestic market comprises both local consumer and visitor spending.

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

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

Diagram 1.2 : Private consumption expenditure held up particularly well

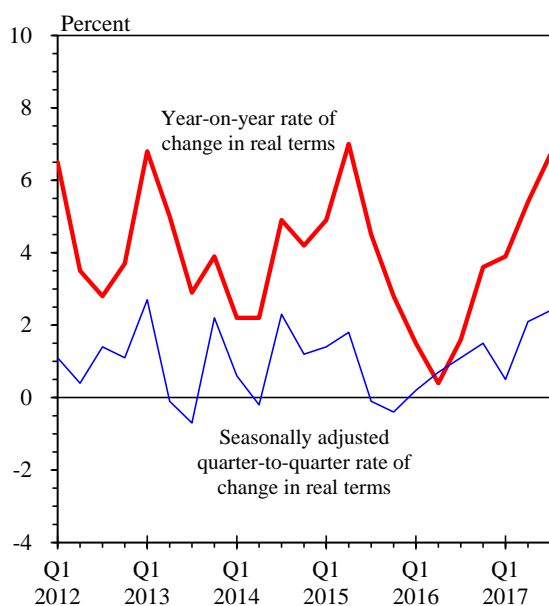
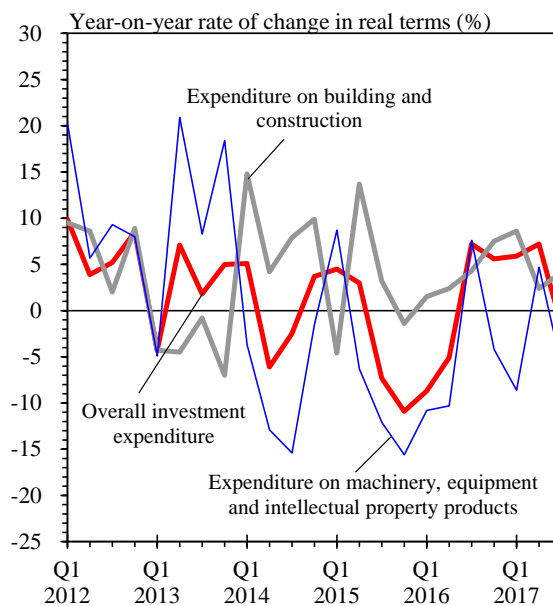


Diagram 1.3 : Overall investment spending recorded a modest decline



1.7 Overall investment spending in terms of *gross domestic fixed capital formation* reverted to a modest decline of 1.7% year-on-year in real terms in the third quarter, following the marked growth of 6.6% in the first half of the year. The decline in the third quarter was due partly to a decrease in machinery and equipment acquisition, a volatile component, and partly to the notable fall in costs of ownership transfer amid a visible slowdown in property market transactions on a year-on-year basis of comparison. Nevertheless, overall building and construction expenditure accelerated to show solid growth, as building and construction works in the public sector accelerated markedly and those in the private sector continued to grow. Also, recent surveys including the latest Quarterly Business Tendency Survey indicated that business sentiment in many economic sectors remained positive (see **Box 1.1** for more detailed analysis of the results of these surveys on business sentiments).

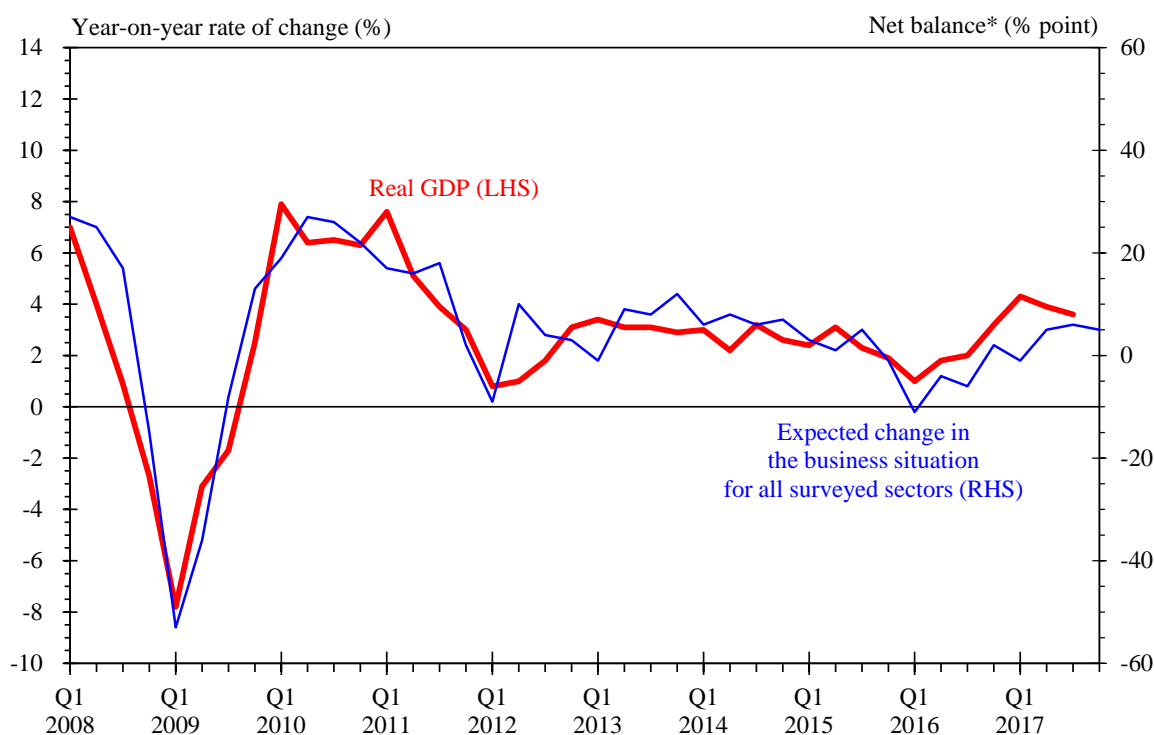
Box 1.1

Business sentiment in Hong Kong

This box article intends to give a general overview of the prevailing business sentiment in Hong Kong, based on results from various surveys that are available in the public domain.

According to the latest results from the Census and Statistics Department (C&SD)'s Quarterly Business Tendency Survey (QBTS)⁽¹⁾, large enterprises in Hong Kong have remained sanguine about their near-term business prospects as the economy sustained above-trend growth in the third quarter of 2017 (*Chart 1*). In particular, the proportion of large enterprises surveyed in early September till mid-October 2017 expecting their business situation to be better in the fourth quarter of 2017 outweighed that of those expecting a weaker business performance by 5 percentage points (i.e. a net balance of +5), broadly similar to the net balances in the preceding two quarters. Among the various sectors, business prospects for large enterprises in “retail” and “accommodation and food services” improved notably and reverted to strong positive net balances (*Table 1*), buttressed by the optimistic local consumer sentiment amid a full-employment situation and the recovery in inbound tourism. Meanwhile, large enterprises in “professional and business services” and “import/export trade and wholesale” turned somewhat more upbeat regarding the near-term outlook, and those in “information and communications”, “financing and insurance” and “real estate” remained optimistic. On the other hand, business sentiment of large enterprises in “manufacturing”, “construction”, “transportation, storage and courier services” weakened somewhat from a quarter earlier. Hiring sentiment of large enterprises in most sectors remained positive (*Table 2*), broadly in line with the prevailing robust growth in employment.

Chart 1 : Large enterprises in Hong Kong remained positive about their near-term business prospects



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

(1) The Quarterly Business Tendency Survey collected views from around 560 large establishments on their near-term business outlook. Respondents were asked to exclude seasonal influences in their responses.

Box 1.1 (Cont'd)

Table 1 : Business sentiment for large enterprises in consumption- and tourism-related segment improved visibly

QBTS: Expected changes in business situation						
	Net balance* (% point)					
	2016		2017			
	Q3	Q4	Q1	Q2	Q3	Q4
Manufacturing	-2	+2	+18	+14	+18	-1
Construction	-12	-11	-18	-14	-9	-16
Import/export trade and wholesale	-14	-14	-6	-2	0	+1
Retail	-38	-2	-15	-4	-4	+24
Accommodation and food services	-11	+13	-14	-13	-2	+13
Transportation, storage and courier services	+5	+12	+7	-2	+2	-7
Information and communications	+12	+15	0	+19	+17	+16
Financing and insurance	+6	+12	+12	+24	+19	+13
Real estate	-3	+4	-2	0	+6	+6
Professional and business services	-14	+9	-8	0	0	+7

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

Table 2 : Hiring sentiment among large enterprises remained largely favourable

QBTS: Expected changes in number of persons engaged						
	Net balance* (% point)					
	2016		2017			
	Q3	Q4	Q1	Q2	Q3	Q4
Manufacturing	+12	+17	+10	-7	+21	+13
Construction	+11	+4	-8	0	+2	-9
Import/export trade and wholesale	-6	-5	0	+2	-1	+1
Retail	-4	+4	+1	+4	-3	+3
Accommodation and food services	+15	+16	+5	+9	+20	+5
Transportation, storage and courier services	+18	+20	+17	+9	+7	+2
Information and communications	+21	+13	+14	+24	+9	+10
Financing and insurance	+10	+10	+15	+16	+16	+13
Real estate	+6	+27	+28	+18	+14	+18
Professional and business services	-7	+15	0	+6	-3	+5

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

Separately, the C&SD also compiled a set of diffusion indices on a monthly basis⁽²⁾ to gauge the general directions of change in the views of small and medium-sized enterprises (SMEs) on their business situation versus the preceding month. The overall index on business receipts since July 2017, despite still below the 50.0 mark, was generally higher than its levels in late-2016 and the first half of 2017 (*Table 3*). Also, the feedbacks from those SMEs consulted continued to suggest a broadly stable employment situation and highly accommodative credit situation in recent months.

Table 3 : Selected results from C&SD's Report on Monthly Survey on the Business Situation of SMEs

	2016			2017									
	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct
Diffusion indices [^] for all selected sectors*													
Business receipts	46.3	46.4	45.2	46.0	46.1	47.2	47.0	47.0	46.5	47.8	48.2	48.5	48.0
Employment	49.3	49.8	49.2	49.7	49.5	49.6	49.7	50.0	49.2	49.0	49.0	49.4	49.8
Percentage of SMEs in all selected sectors*													
with current credit need	9.2	9.4	9.8	8.4	8.5	7.8	8.0	8.1	7.9	7.1	7.2	7.1	7.5
reported tight access to credit ^{&}	0.7	0.6	0.5	0.2	0.1	0.7	0.5	0.1	0.2	0.6	0.1	0.6	0.9

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 / employment situation 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.

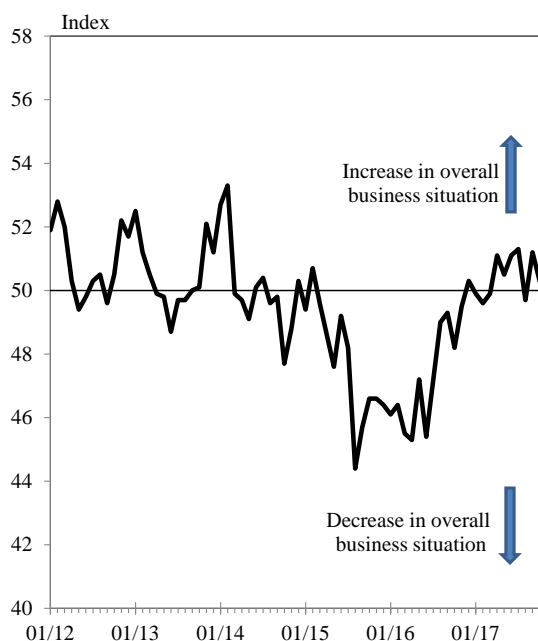
(&) It should be noted that the assessment of credit access situation might display great fluctuations from month to month given the small number of SMEs involved, as a great majority of SMEs reported "no credit need". Thus the results should be interpreted with caution.

(2) It refers to the results from the Monthly Survey on the Business Situation of SMEs that solicits feedbacks from a panel sample of around 600 SMEs each month.

Box 1.1 (Cont'd)

As for other surveys in the public domain, the Nikkei Purchasing Managers' Index (PMI) of Hong Kong⁽³⁾, which gauges the performance of the private sector's business activity, has stayed above the 50.0 divide in most of the months since the second quarter of 2017 (*Chart 2*), signalling that the overall business situation generally saw further improvement amid the generally sanguine global economy. Separately, the Hong Kong Trade Development Council (HKTDC)'s Export Index⁽⁴⁾, though easing somewhat in the third quarter from its four-year high in the preceding quarter, was still notably higher than the readings reported in 2016 (*Table 4*).

Chart 2 : Nikkei Hong Kong PMI pointed to stabilised business sentiment



Sources: Nikkei; IHS Markit.

Note: A reading above 50 indicates an increase in the overall business situation, whereas a reading below 50 indicates a decrease in the overall business situation. The index has been adjusted for seasonality.

Table 4 : HKTDC's Export Index

2015	Q1	44.9
	Q2	46.8
	Q3	37.1
	Q4	31.4
2016	Q1	37.3
	Q2	37.2
	Q3	38.8
	Q4	33.7
2017	Q1	47.1
	Q2	50.1
	Q3	46.2

Source: HKTDC.

Note: A reading above 50 indicates that more than half of the surveyed traders incline towards the upside, which can be interpreted as an upward trend and an increase in confidence, and vice versa for a reading below 50.

It is worthwhile to point out that these surveys are essentially opinion-based, thereby unavoidably subject to various limitations (e.g. results are not directly comparable) and hence the results should be interpreted with care. Still, the latest survey findings seem to suggest that business sentiment in Hong Kong has remained positive of late, as the global economy is generally expected to expand moderately further in the near term. That said, with the lingering uncertainties in the external environment, the Government will stay vigilant to the global economic developments and their possible repercussions on the Hong Kong economy.

- (3) According to the press release jointly released by Nikkei and IHS Markit, the Nikkei Hong Kong PMI is compiled according to monthly replies to questionnaires sent to purchasing executives in over 300 companies. It is a composite index based on five individual indices with the following weights: New Orders (0.3); Output (0.25); Employment (0.2); Suppliers' Delivery Times (0.15); and Stock of Items Purchased (0.1), with the Delivery Times index inverted so that it moves in a comparable direction. Survey responses reflect the change, if any, in the prevailing month compared to the previous month.
- (4) The HKTDC Export Index is compiled based on a quarterly survey to collect views from around 500 traders concerning their export performances in the prevailing quarter as well as their outlook for the subsequent quarter and covers six major industries – electronics, clothing, jewellery, timepieces, toys and machinery.

The labour sector

1.8 The labour market remained in a state of full employment. The *seasonally adjusted unemployment rate* held steady at a low level of 3.1% in the third quarter. The *underemployment rate* edged lower to 1.1% in the same quarter. Total employment registered further solid growth in the third quarter. Wages and earnings generally sustained growth in real terms. Benefitting partly from the upward adjustment of the Statutory Minimum Wage rate since May 2017 and partly from a tight labour market, the average monthly employment earnings of full-time employees (excluding foreign domestic helpers) of the lowest decile group continued to increase, by 4.6% year-on-year in real terms in the third quarter.

The asset markets

1.9 The *local stock market* was largely buoyant in the third quarter, alongside rallies in major stock markets overseas. Investor sentiment remained generally upbeat as the global economic outlook improved. The Hang Seng Index closed the third quarter at 27 554, up by 6.9% from the level at the end of the previous quarter. Average daily turnover went visibly higher to \$93.2 billion in the third quarter, from \$77.8 billion in the preceding quarter. Credit growth remained strong. Loans for use in Hong Kong (including trade finance) at end-September increased by 15.2% over a year earlier, compared to that of 13.8% at end-June.

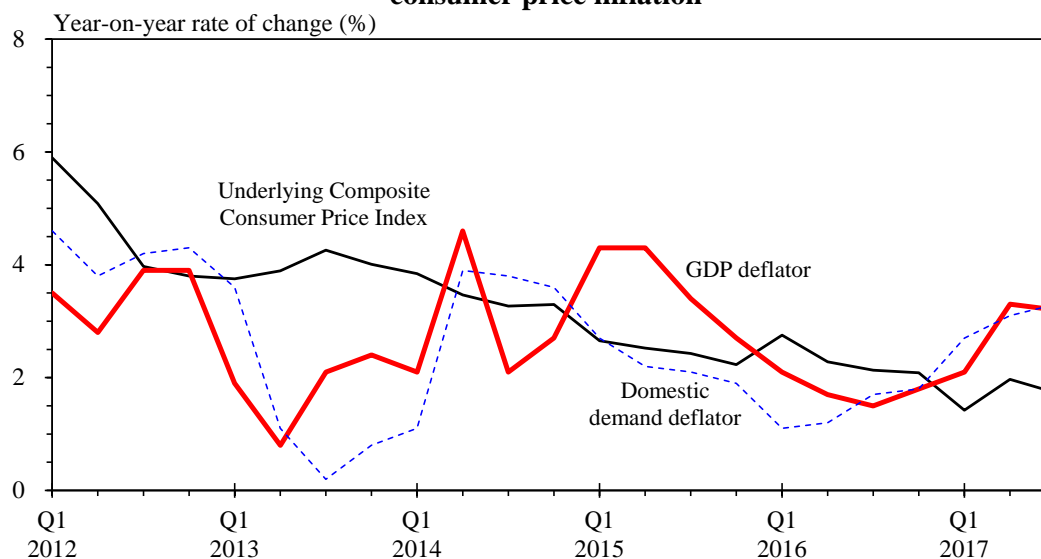
1.10 The *residential property market* continued to show moderation in the third quarter, extending the trend that began in June. Trading activities slowed down visibly from the hectic level in the preceding quarter, with the number of residential property transactions falling from 18 900 in the second quarter to 13 200 in the third quarter. Residential property prices recorded a decelerated increase of 1% between June and September. Yet, compared to the 1997 peak, overall flat prices in September were still 97% higher. Meanwhile, the housing affordability ratio worsened to around 68% in the third quarter. During the third quarter, flat rentals rose by 2%, and shop and office rentals also increased, by 1% and 2% respectively.

Inflation

1.11 Consumer price inflation eased in the third quarter. Netting out the effects of the Government's one-off relief measures to more accurately reflect the underlying inflation trend, *underlying composite consumer price inflation* was 1.7% in the third quarter, lower than that of 2.0% in the second quarter. Meanwhile, *headline consumer price inflation* also eased to 1.8%. External price pressure remained modest, thanks to the mild inflation in our major import sources. Local cost pressures stayed contained, as the labour cost pressures were modest when viewed against the sustained expansion of economic output at an above-trend pace. Rental cost pressures as reflected in consumer price inflation were broadly moderate as well, as the feed-through from the general uptrend in fresh-letting residential rentals since the second quarter of 2016 was only gradual. The launch of some new government subsidies to education in the 2017-18 academic year, together with dissipation of the effect from upward adjustment in public housing rentals in September last year, also contributed to the more discernible easing of the inflation rate in September 2017.

1.12 The year-on-year rate of increase in the *GDP deflator* was 3.2% in the third quarter, broadly similar to that in the preceding quarter. Analysed by major components, the year-on-year rate of increase of the domestic demand deflator was broadly similar to that in the preceding quarter, while the terms of trade continued to hold virtually unchanged year-on-year.

Diagram 1.4 : Inflation remained moderate in the third quarter, with some easing in consumer price inflation



Note : The year-on-year rates of change of the Composite Consumer Price Index from the fourth quarter of 2015 onwards are computed from the new 2014/15-based series, and those before are from the old 2009/10-based series.

GDP by major economic sector

1.13 The net output of the services sector as a whole expanded solidly by 3.1% year-on-year in real terms in the second quarter of 2017, with various degrees of expansion in all key service industries. Among them, import and export trade as well as transportation and storage registered further visible growth in net output, mirroring the active regional trade and cargo flows. Amid the improvement in inbound tourism, the net output of wholesale and retail trades reverted to growth after seven consecutive quarters of decline, whereas that of the accommodation and food services maintained some modest growth. The net output of real estate sector, which covers activity of private sector developers and property agencies, expanded at a moderated pace. The net output of financing and insurance, and information and communications continued to see solid growth, whereas that of professional and business services grew modestly further. As for the secondary sector, the net output of construction sector expanded solidly amid sustained expansion in infrastructure and building works. Manufacturing continued to see some marginal increase in its net output.

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

	<u>2016</u>	<u>2016</u>				<u>2017</u>	
		<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
Manufacturing	-0.4	-0.3	-0.4	-0.1	-1.0	0.2	0.4
Construction	2.6	-1.2	0.8	3.0	7.6	8.6	3.4
Services ^(b)	2.3	1.6	2.7	2.3	2.5	3.5	3.1
Import/export, wholesale and retail trades	0.4	-2.1	0.9	0.8	1.7	3.9	3.5
Import and export trade	2.1	0.1	2.8	2.3	2.9	5.1	4.2
Wholesale and retail trades	-6.0	-10.0	-5.9	-5.9	-2.8	-0.8	0.6
Accommodation ^(c) and food services	0.1	-0.9	1.0	0.1	0.2	1.6	1.2
Transportation, storage, postal and courier services	3.3	2.6	3.4	3.5	3.8	4.7	4.8
Transportation and storage	3.4	2.8	3.5	3.4	3.8	4.5	4.5
Postal and courier services	2.3	-1.4	2.7	5.8	2.5	9.0	9.4
Information and communications	3.7	3.7	4.2	3.7	3.3	3.8	3.4
Financing and insurance	4.7	5.0	4.2	4.7	4.8	5.2	4.9
Real estate, professional and business services	3.0	1.8	3.7	3.2	3.5	4.4	2.1
Real estate	3.7	0.6	2.9	5.5	6.0	8.5	3.7
Professional and business services	2.5	2.6	4.4	1.4	1.7	0.6	0.8
Public administration, social and personal services	2.7	2.5	3.3	2.5	2.3	2.5	2.6

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, while those shown in Table 1.1 are compiled from the expenditure approach. For details, see Note (2) 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.
- (c) Accommodation services cover hotels, guesthouses, boarding houses and other establishments providing short-term accommodation.

Other economic developments

1.14 Hong Kong was ranked as the world's freest economy by the Fraser Institute in September. Of the five broad areas of assessment, Hong Kong continued to attain high rankings in "regulation" (first) and "freedom to trade internationally" (second). Hong Kong has maintained the top position since the Institute published its first report in 1996. This is a clear recognition of the Government's unswerving commitment to upholding economic freedom and to sustaining a favourable business environment. Separately, in terms of overall competitiveness, Hong Kong leapt three places to reach the sixth place worldwide in the World Economic Forum's Global Competitiveness Report 2017–2018 released in the same month.

1.15 The Chief Executive delivered the 2017 Policy Address in October 2017, which outlined the current-term Government's vision on various policy areas, and put forward measures with new perspectives to promote economic development and enhance people's livelihood. The more salient points on economic development are highlighted below.

- The Government will seize the opportunities from the Belt and Road Initiative and the Guangdong-Hong Kong-Macao Bay Area development. In particular, for the Belt and Road Initiative, the Government will continue discussion with the Central Authorities with the aim of entering into an agreement of Hong Kong's full participation in the Initiative with the National Development and Reform Commission as soon as possible.
- The Government will introduce two new tax measures to enhance Hong Kong's competitiveness. First, under the proposed two-tier profits tax system to provide tax relief to small and medium-sized enterprises, the profits tax rate will be lowered to 8.25% for the first \$2 million of profits, with standard tax rate at 16.5% for profits exceeding that amount. Second, under a proposal to encourage research and development (R&D) investment by enterprises, a 300% tax deduction for the first \$2 million eligible R&D expenditure will be introduced, with the remainder at 200%.
- In order to meet the needs arising from economic development, the Government will continue to increase the supply of various types of land, including general industrial/commercial sites, sites for logistics use, and sites for convention and exhibition facilities. To tackle the housing problem, the Government will take a multi-pronged approach and make sustained efforts to develop land, build a housing ladder focusing on home-ownership, and facilitate the implementation of short-term community initiatives to increase the supply of transitional housing.

- The Government will continue to devote new resources in education for Hong Kong's sustained development. The Government will also set up task forces to further review eight key areas of education⁽⁴⁾. Furthermore, the Government will set up the Commission for the Planning of Human Resources, to ensure that our human resources will cater for the development needs of Hong Kong and keep up with our country's latest developments as well as the evolving trends in the global market.
- The Government will step up its efforts to develop innovation and technology as a new model of development, through various measures such as setting aside no less than \$10 billion as university research funding, kick-starting the \$500 million "Technology Talent Scheme" to train and pool technology talent, injecting \$3 billion into the Research Endowment Fund to provide studentships for local students admitted to research postgraduate programmes funded by the University Grants Committee, and deploying \$2 billion under the Innovation and Technology Venture Fund Scheme to co-invest with venture capital funds in local technology start-ups.

Notes :

- (1) The table below presents a more detailed comparison between the growth forecasts made by the IMF in October 2017 and those made three months ago.

	<u>2016</u>	<u>July round</u>	<u>2017</u> <u>October round</u>
	(%)	(%)	(%)
World (PPP ^{##} weighted)	3.2	3.5	3.6
Advanced economies	1.7	2.0	2.2
US	1.5 [#]	2.1	2.2
Euro area	1.8 [#]	1.9	2.1
UK	1.8 [#]	1.7	1.7
Japan	1.0 [#]	1.3	1.5
Emerging market and developing economies	4.3	4.6	4.6
Emerging and developing Asia	6.4	6.5	6.5
Mainland China	6.7 [#]	6.7	6.8
India [^]	7.1 [#]	7.2	6.7

- Notes : (#) Actual figures.
 (^) Fiscal year.
 (##) PPP refers to purchasing power parity.

- (2) 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.
- (3) 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 by summing up its main components.
- (4) The eight key areas of education to be reviewed include professional development of teachers, curriculum arrangement, assessment system, vocational and professional education and training, self-financing post-secondary education, school-based management, parent education and University Grants Committee's funding on research and student hostels.