

Outlook for the Hong Kong economy in 2008

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

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

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

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

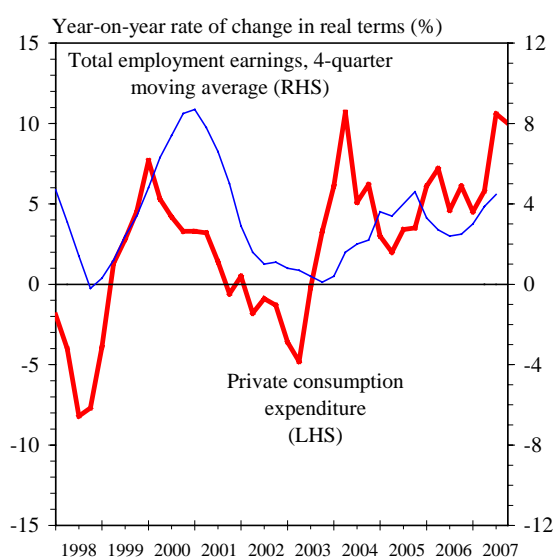


2.19 Locally, both consumer and investor confidence should hold up firmly. The strong economic upturn over the past four years, as well as the rises in household income and wealth, have strengthened the willingness of consumers to spend. Yet the uncertainty in the performance of the asset markets in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

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

Diagram 2.6 : Consumer confidence likely to stay strong

(a) Sustained improvement in employment conditions is a plus factor



(b) Lower interest rates also help

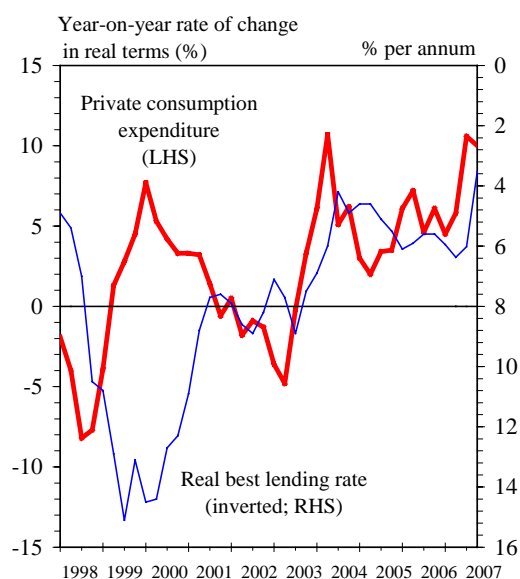


Diagram 2.7 : Consumer sentiment will also depend on asset market performance

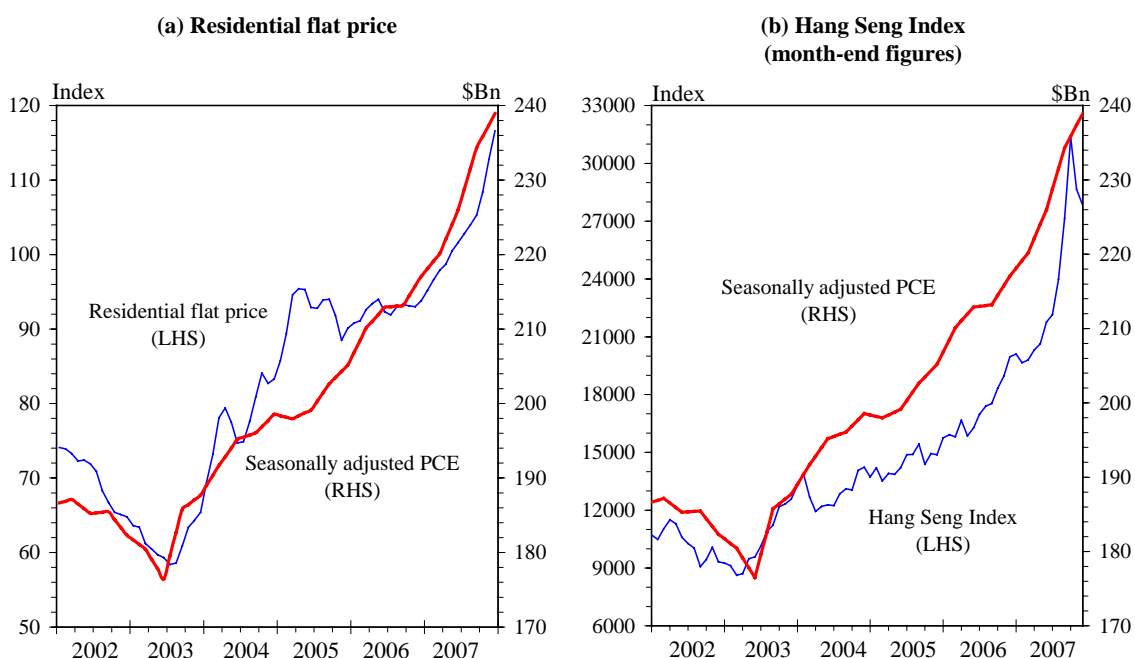
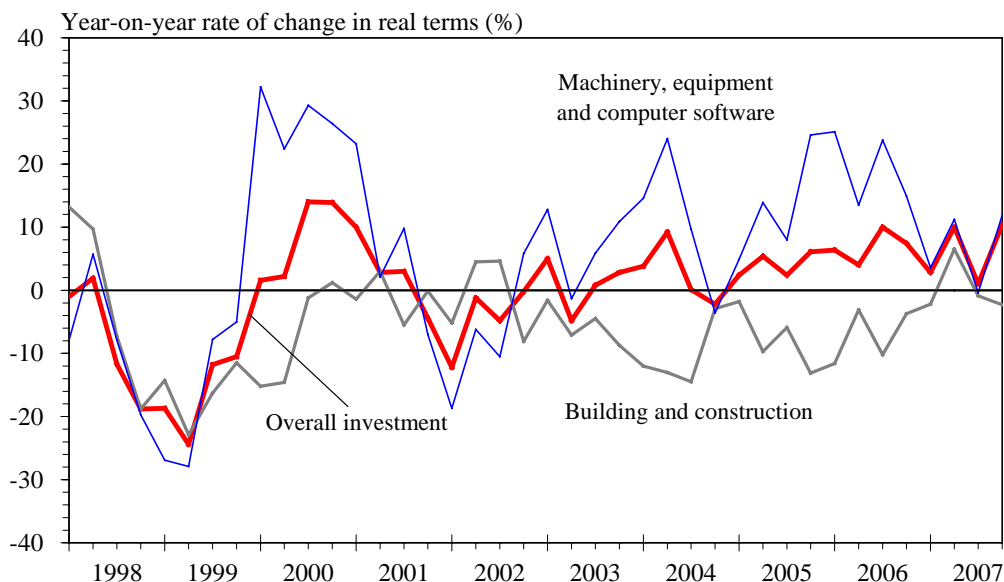


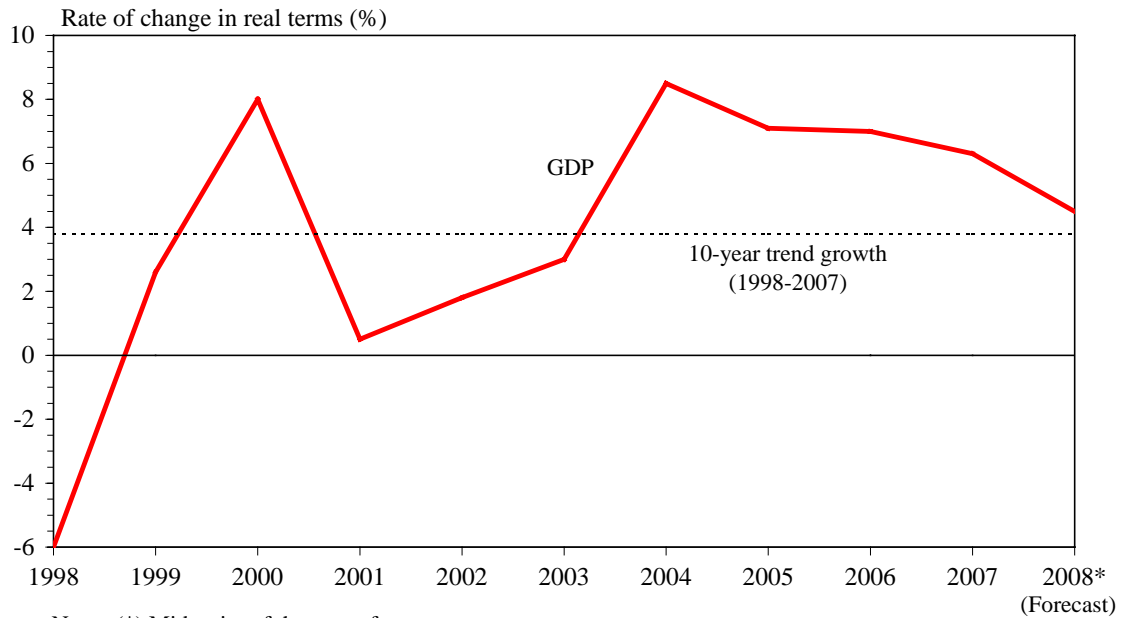
Diagram 2.8 : Integration with the Mainland should induce further investment activities



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

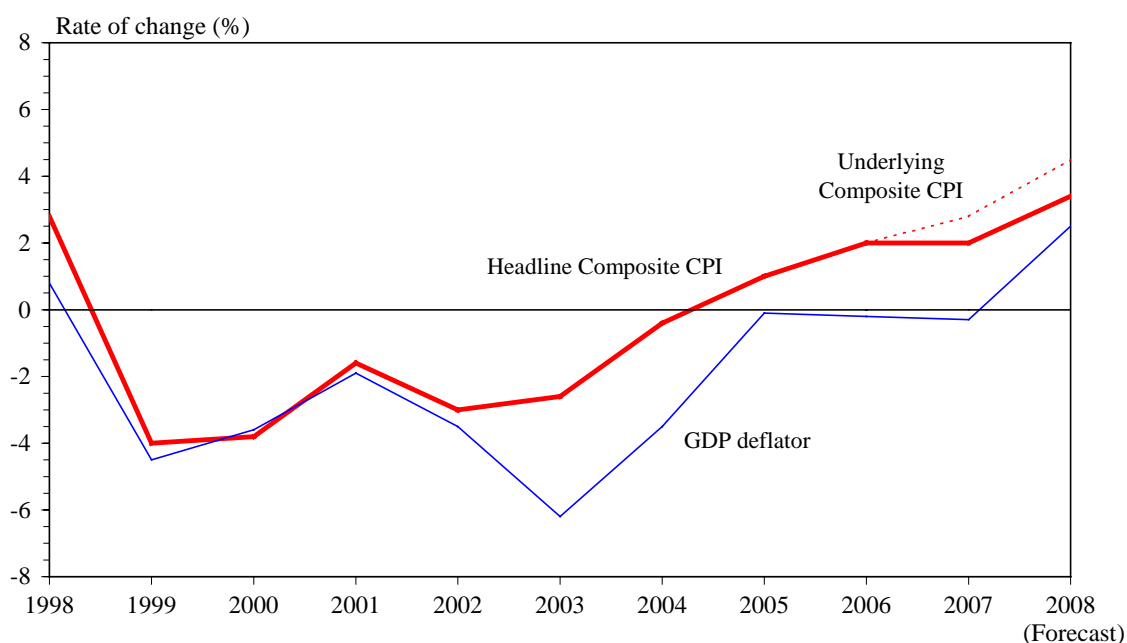
private sector, which generally suggest a further solid expansion of the Hong Kong economy at a pace mostly in the range of 4.5–5.5%.

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



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

Diagram 2.10 : Inflation will go up further in 2008



Forecast rate of change in 2008 (%)

Gross Domestic Product (GDP)

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

Composite Consumer Price Index

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

GDP Deflator	2.5
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