

Press Release

(embargoed until 4:15 p.m. on 16 May 2008)

Economic Situation in the First Quarter of 2008 and Latest GDP and Price Forecasts for 2008

The Government released today (Friday) the First Quarter Economic Report 2008, together with the preliminary figures on Gross Domestic Product for the first quarter of 2008.

The Government Economist, Mr K C Kwok, described the economic situation in the first quarter of 2008 and provided the latest GDP and price forecasts for the year.

MAIN POINTS

- * The Hong Kong economy continued to expand strongly in the first quarter of 2008, despite the growing adversities in the external environment. With real GDP growing by 7.1%, the economy extended the run of distinctly above-trend growth to 18 quarters.
- * The external sector stayed resilient to the increasingly challenging environment in the first quarter, which was characterised by a weakening US economy and financial market turbulence. Total exports of goods attained further notable growth of 8.3% in real terms in the first quarter, supported by the vibrant performance of the Mainland and other emerging economies and the further expansion of the EU market. Exports of services also stayed strong in the first quarter, growing rapidly further by 10.8% in real terms on the back of a continued surge in financial services, as well as notable growth in offshore trade and inbound tourism.
- * Domestically, both consumer and investor confidence remained strong in the first quarter, thus maintaining domestic demand's key role in supporting overall economic growth. Private consumption expenditure rose markedly further by 7.9% in real terms, underpinned by the firm labour market conditions and rising incomes. Overall investment held up well, expanding by 8.9% in real terms with a rebound in building and construction activity. However, amidst dimmer global economic prospects, the local stock market experienced further consolidation in the first quarter and the housing market turned less hectic.
- * Labour market conditions continued to be firm in the first quarter. The seasonally adjusted unemployment rate remained stable at 3.4%, and the underemployment rate fell further to a ten-year low of 1.9%. Labour earnings and wages were on the rise.
- * Consumer price inflation picked up further in the first quarter, mostly due to the surge in food prices amidst the global food inflation. The sustained above-trend economic growth also added to inflationary pressure from the

demand side. Headline Composite CPI inflation averaged at 4.6% in the first quarter. After netting out the one-off effects of the rates concession this year and the public housing rental waiver last year, underlying Composite CPI inflation in the first quarter was 4.9%.

- * Looking ahead, the external environment will remain uncertain and challenging. The US economy will continue to be weak with the effects of the housing market downturn spreading into the wider economy, while global financial markets are likely to remain unsettled. Economic activities in other major advanced economies have also showed signs of deceleration.
- * Nevertheless, the growth momentum in the emerging and developing economies, including the Mainland economy, is expected to remain vibrant, although there should unavoidably be some mild moderation in growth due to the weaker demand from the advanced economies. Yet this should still provide some cushioning effect to the impact of the economic slowdown in the developed world on Hong Kong in the coming quarters.
- * Domestic demand is expected to grow solidly further and remain a key driver in economic growth going forward. The firm labour market conditions and rising incomes should continue to give strength to private consumption. As business confidence holds up well and interest rates remain low, there should also be further growth in investment spending in the rest of the year.
- * Overall, given the uncertainties prevailing in the external environment and dimmer global economic prospects, the GDP forecast at 4-5% as announced in the Budget round in February is kept unchanged. Yet with the strong GDP growth in the first quarter, and barring any abrupt external shocks, it is likely that GDP growth in 2008 should be close to the upper end of the range forecast.
- * The inflation outlook is likewise rather uncertain and will hinge much on the movements of food prices in the international markets in the rest of the year, which can be expected to be volatile. Apart from global food prices, the elevated international oil prices, the exchange rate movements as well as the strength of the local economy are likely to continue to exert inflationary pressure. Nevertheless, the sustained increase in labour productivity will provide some offsetting effect. In view of the high degree of uncertainties in the external environment, the forecast rate of increase in the underlying Composite CPI for 2008 is maintained at 4.5%. The corresponding forecast headline inflation rate is also kept unchanged at 3.4%. The risks to these forecasts are on the upside. The Government will review the inflation forecast as more incoming data become available.

DETAIL

GDP

According to the preliminary figure on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, GDP expanded strongly further by 7.1 % in real terms in the first quarter of 2008 over a year earlier. By now, the economy extended the run of distinctly above-trend growth to 18 quarters. Consumption expenditure rose markedly, investment spending held up well, and exports of goods and services grew notably further. On a seasonally adjusted quarter-to-quarter comparison, GDP also grew strongly further, by 1.8% in real terms in the first quarter of 2008 (*Chart*).

2. The latest figures on GDP and its major expenditure components up to the first quarter of 2008 are presented in *Table 1*. Developments in different segments of the economy in the first quarter of 2008 are described below.

External trade

3. External trade stayed resilient to the increasing adversities in the trading environment in the first quarter of 2008. *Total exports of goods* registered a notable growth of 8.3% in real terms in the first quarter over a year earlier, supported by the vibrant performance of many emerging markets and the solid expansion of the EU market. On a seasonally adjusted quarter-to-quarter comparison, total exports of goods expanded further by 1.4% in real terms in the first quarter of 2008.

4. *Exports of services* maintained a strong growth of 10.8% in real terms in the first quarter of 2008 over a year earlier. Exports of travel services expanded rapidly further in tandem with the vibrant inbound tourism, and exports of trade-related services continued to benefit from the Mainland's buoyant trade flows. Notwithstanding the global financial turbulence, exports of financial services grew strongly further, albeit slightly moderated from its earlier hectic pace of expansion. On a seasonally adjusted quarter-to-quarter comparison, exports of services grew by 1.1% in the first quarter of 2008.

Domestic sector

5. Domestic demand continued to play an important role in driving economic growth. Local consumer spending remained strong in the first quarter, with consumer sentiment being well supported by the firm labour market conditions and rising incomes. *Private consumption expenditure (PCE)* rose markedly by 7.9% in real terms in the first quarter, similar to the growth in 2007 as a whole. On a seasonally adjusted quarter-to-quarter comparison, private consumption expenditure fell slightly by 0.1% in the first quarter.

6. *Overall investment spending* accelerated, expanding by 8.9% in real terms in the first quarter of 2008. Machinery and equipment investment continued to rise notably by 6.0% in the first quarter, along with the continued expansion of general economic activity. Indeed, the results of latest Quarterly Business Tendency Survey conducted by the Census and Statistics Department indicated that large business establishments were largely optimistic about the near-term business situation. Private sector activity in the construction sector rose modestly in the first quarter, while public sector activity rebounded notably from a low base. Taking altogether, overall expenditure on building and construction increased solidly by 5.2% in the first quarter of 2008. Also, the active property market led to a sharp increase in ownership transfers.

The labour sector

7. Labour market conditions continued to be firm in the first quarter, underpinned by the strong economic expansion. The *seasonally adjusted unemployment rate* remained stable at 3.4%, and the *underemployment rate* fell further to 1.9%, a ten-year low. Increases in labour earnings and wages were experienced across-the-board in 2007, and became more notable in the fourth quarter of 2007.

Prices

8. *Underlying consumer price inflation* accelerated further to an average of 4.9% in the first quarter, mostly due to the surge in food prices and the faster increase in private housing rentals. The sustained above-trend economic growth also added to inflationary pressure from the demand side. *Headline consumer price inflation*, having taken all the relevant one-off measures into account, was 4.6%, slightly lower than its underlying counterpart in the first quarter as the low base effect created by the public housing rental waiver in February 2007 had offset most of the alleviation effect from the rates concession in the first quarter of 2008. On top of surging food prices and faster rental increases, inflationary pressure was also sustained by the elevated energy prices, gradual appreciation of the renminbi and the weak US dollar, as well as the rising labour costs. As to the *GDP deflator*, a slower increase of 2.3% was recorded in the first quarter, due to the less favourable terms of trade.

Latest GDP and price forecasts for 2008

9. Looking ahead, the external environment will remain uncertain and challenging. The US economy will continue to be weak with the effects of the housing market downturn spreading into the wider economy, while global financial markets are likely to remain unsettled. Economic activities in other advanced economies have also showed signs of deceleration.

10. Nevertheless, the growth momentum in the emerging and developing economies, including the Mainland economy, is expected to remain vibrant, although there should unavoidably be some mild moderation in growth due to the weaker demand from the advanced economies. Yet this should still provide some cushioning effect to the impact of the economic slowdown in the developed world on Hong Kong in the coming quarters. However, the effects of the macro-tightening measures in the Mainland need to watch closely.

11. Domestic demand is expected to grow solidly further and remain a key driver in economic growth going forward. The firm labour market conditions and rising incomes should continue to give strength to private consumption. As business confidence holds up well and interest rates remain low, there should also be further growth in investment spending in the rest of the year.

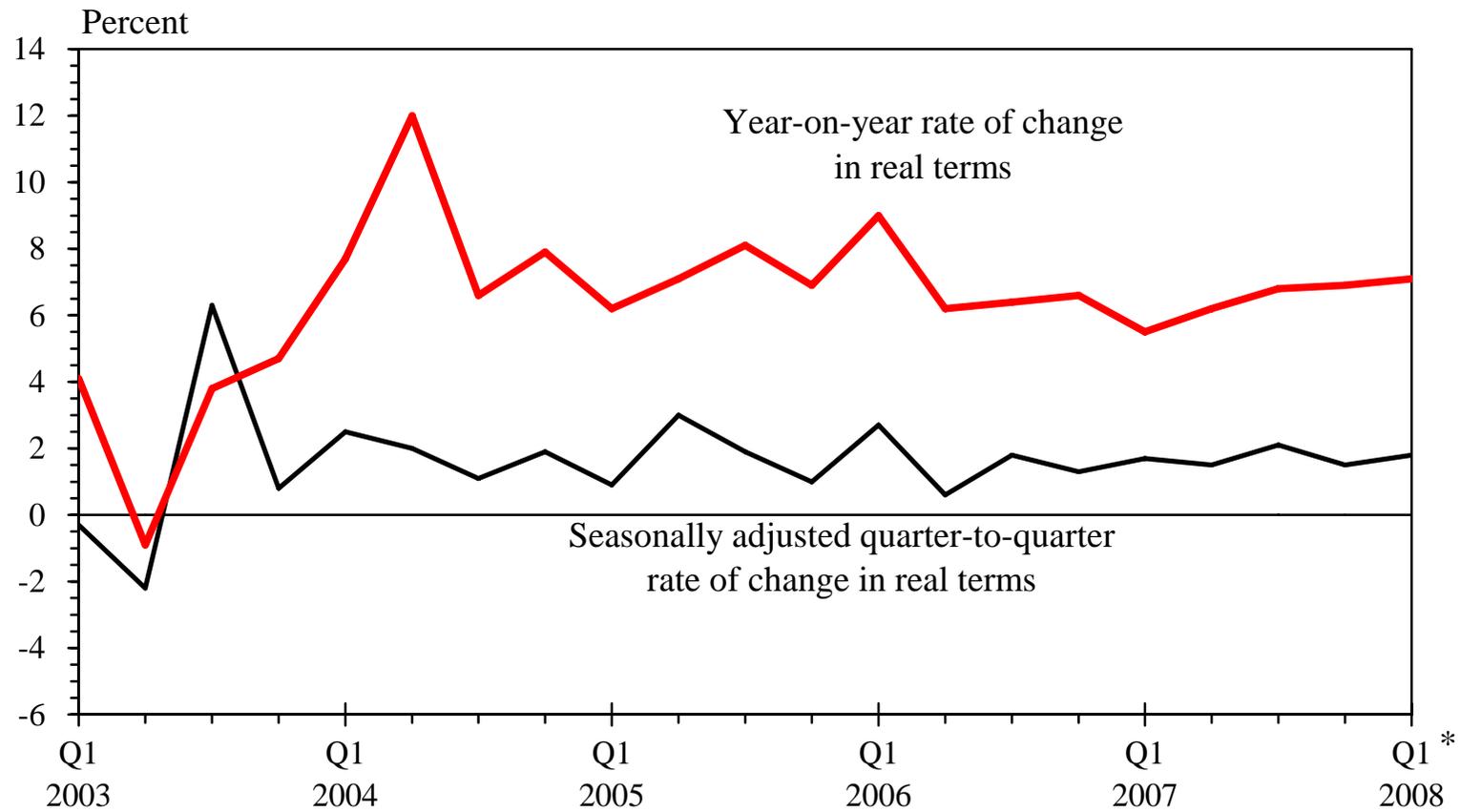
12. Overall, given the uncertainties prevailing in the external environment and dimmer global economic prospects, the GDP forecast at 4-5% as announced in the Budget round in February is kept unchanged. Yet with the strong GDP growth in the first quarter, and barring any abrupt external shocks, it is likely that GDP growth in 2008 should be close to the upper end of the range forecast (*Table 2*). For comparison, the forecasts of Hong Kong's GDP growth by a selection of international organisations and local analysts are summarised in *Table 3*.

13. The inflation outlook is likewise rather uncertain and will hinge much on the movements of food prices in the international markets in the rest of the year, which can be expected to be volatile. Apart from global food prices, the elevated international oil prices, the exchange rate movements as well as the strength of the local economy are likely to continue to exert inflationary pressure. Nevertheless, the sustained increase in labour productivity will provide some cushioning effect. In view of the high degree of uncertainties in the external environment, the forecast rate of increase in the underlying Composite CPI for 2008 is maintained at 4.5%. The corresponding forecast headline inflation rate is also kept unchanged at 3.4%. The risks to these forecasts are on the upside. The Government will review the inflation forecast as more incoming data become available.

(The First Quarter Economic Report 2008 is now available. Users can download the publication free of charge at <http://www.statisticalbookstore.gov.hk> or <http://www.info.gov.hk/hkecon/report>. Print version of the report can also be purchased on-line, or by calling the Publications Sales Unit of ISD at 2537 1910. The hard copy of the report is available for sale at \$67 per copy (15% discount offered if purchased on-line), with a postage charge.)

(The GDP figures up to the first quarter of 2008 are published in the Report of the Gross Domestic Product, First Quarter 2008. Users can download the publication free of charge at <http://www.statisticalbookstore.gov.hk>. Print version of the report can also be purchased on-line, or by calling the Publications Sales Unit of ISD at 2537 1910. The hard copy of the report is available for sale at \$47 per copy (15% discount offered if purchased on-line), with a postage charge.)

Hong Kong's Gross Domestic Product



Note : (*) Preliminary figures.

Table 1

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

	<u>2006[#]</u>	<u>2007[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>2007</u> <u>Q3[#]</u>	<u>Q4[#]</u>	<u>2008</u> <u>Q1⁺</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>							
Private consumption expenditure	6.0	7.8	4.5 (1.5)	6.6 (3.0)	10.6 (3.2)	9.5 (1.6)	7.9 (-0.1)
Government consumption expenditure	0.1	2.3	2.3 (1.6)	3.0 (-0.3)	1.5 (-0.3)	2.3 (1.2)	0.3 (-0.4)
Gross domestic fixed capital formation	7.0	4.2	0.8	8.1	-0.5	8.2	8.9
<i>of which :</i>							
Building and construction	-7.3	1.0	-1.9	7.3	-0.2	-1.2	5.2
Machinery, equipment and computer software	19.1	3.5	0.3	7.8	-2.7	8.5	6.0
Total exports of goods	9.3	7.0	6.5 (0.3)	10.0 (3.0)	6.2 (0.2)	5.7 (1.8)	8.3 (1.4)
Imports of goods	9.2	8.8	7.1 (0.1)	11.5 (4.1)	8.1 (0.5)	8.5 (3.1)	8.4 (-1.1)
Exports of services	10.1	12.5	11.3 (3.5)	11.6 (2.8)	13.7 (4.2)	13.1 (2.2)	10.8 (1.1)
Imports of services	8.1	8.5	6.6 (0.5)	8.9 (5.8)	8.7 (0.3)	9.7 (2.8)	11.3 (2.2)
Gross Domestic Product	7.0	6.4	5.5 (1.7)	6.2 (1.5)	6.8 (2.1)	6.9 (1.5)	7.1 (1.8)
<i>Change in the main price indicators (%)</i>							
GDP deflator	-0.3	3.0	1.4 (0.6)	2.0 (0.9)	3.2 (1.1)	4.9 (2.1)	2.3 (-1.7)
Composite Consumer Price Index	2.0	2.0	1.7 (*)	1.3 (0.3)	1.6 (0.8)	3.5 (2.2)	4.6 (1.1)
<u>Change in nominal GDP (%)</u>	6.7	9.5	7.0	8.4	10.2	12.1	9.6

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.

(#) Revised figures.

(+) Preliminary figures.

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

(*) Change of less than 0.05%.

Table 2

**Economic forecasts for 2008
(year-on-year rate of change (%))**

	Forecasts for 2008 as released on 27.2.2008 (%)	Latest forecasts for 2008 on 16.5.2008 (%)
Gross Domestic Product (GDP)		
<i>Real GDP</i>	4 to 5	4 to 5
<i>Nominal GDP</i>	6.5 to 7.5	6.5 to 7.5
Composite Consumer Price Index (CCPI)		
<i>Headline CCPI</i>	3.4	3.4
<i>Underlying CCPI</i>	4.5	4.5
GDP Deflator	2.5	2.5

Table 3

2008 GDP and price forecasts for Hong Kong put out by selected international organisations and private sector analysts

	Date of release	GDP (growth rate)	Private consumption expenditure rate	Gross domestic fixed capital Formation in real	Total exports of goods terms	Exports of services (%)	Rate of change in consumer prices (%)	Reference source
International organisations:								
IMF	Oct 2007	4.7	--	--	--	--	3.2	World Economic Outlook, Oct 2007.
	Feb 2008	4.6	3.2	1.7	--	--	3.7	2007 Article IV Consultation -Staff Report, February 2008.
	Apr 2008	4.3	--	--	--	--	3.6	World Economic Outlook, Apr 2008.
ADB	Sep 2007	5.4	--	--	--	--	2.5	Asian Development Outlook 2007 Update, Sep 2007.
	Apr 2008	4.5	--	--	--	--	3.4	Asian Development Outlook 2008, Apr 2008.
PECC	Dec 2007	6	--	--	--	--	2.87	State of the Region 2007-2008, 13 Dec 2007.
World Bank	Nov 2007	5.2	--	--	--	--	--	East Asia and Pacific Update, Nov 2007.
	Apr 2008	4.8	--	--	--	--	--	East Asia and Pacific Update, Apr 2008.
United Nations	Jan 2008	5.7	--	--	--	--	1.4	World Economic Situation and Prospects 2008, 9 Jan 2008.
United Nations, ESCAP	Mar 2008	5.7	--	--	--	--	3.4	Economic and Social Survey of Asia and the Pacific 2008, Mar 2008.
Private sector analysts:								
<i>(a) Major local banks</i>								
HSBC	Jan 2008	5	5.3	7.6	--	--	3.9	Macro Asia Economics Q1 2008, 8 Jan 2008.
	Mar 2008	5	7.6	7.6	--	--	3.9	Macro Asia Economics Q2 2008, 27 Mar 2008.
Hang Seng Bank	Nov 2007	5	--	--	--	--	3.8	Hang Seng Bank, 12 Nov 2007.
	Feb 2008	5	--	--	--	--	3.5	Hong Kong Economic Monitor, February 2008.
	May 2008	5	--	--	--	--	4	Hang Seng Bank, 13 May 2008.
Standard Chartered Bank	Dec 2007	5.2	--	--	--	--	3.6	Oriental Daily News, 29 Dec 2007.
	Feb 2008	4.6	--	--	--	--	3.8	Standard Chartered Global Focus, 21 Feb 2008.
	May 2008	4.6	--	--	--	--	Headline: 4.1 Underlying : 5.2	Standard Chartered Bank, 13 May 2008.

Table 3 (cont'd)

2008 GDP and price forecasts for Hong Kong put out by selected international organisations and private sector analysts

	Date of release	GDP (growth rate)	Private consumption expenditure rate	Gross domestic fixed capital formation		Total exports of goods terms	Exports of services (%)	Rate of change in consumer prices (%)	Reference source
				in	real				
Bank of China (HK)	Dec 2007	5	5.5	4.5		7.6	9.8	3.5	Economic Review, Dec 2007.
	May 2008	5	5.5	4.5		7.6	9.8	4.5	Economic Review, May 2008.
Bank of East Asia	Jan 2008	5	7.5	4.5		6	8.5	3.5	Economic Analysis, Jan 2008.
	Mar 2008	4.5	6.5	--		7	--	3.5	Wen Wei Po, 20 Mar 2008.
	May 2008	4.5	--	--		--	--	4	Bank of East Asia, 13 May 2008.
Citigroup	Dec 2007	6.2	--	--		--	--	3.3	Oriental Daily News, 29 Dec 2007.
	Jan 2008	5.3	6	7.2		--	--	3.7	Asia Economic Outlook and strategy, 28 Jan 2008.
	Apr 2008	4.5	6.1	7		--	--	3.7	Asia Economic Outlook and strategy, 29 Apr 2008.
<i>(b) Investment banks</i>									
Goldman Sachs Asia	Nov 2007	6	--	--		--	--	4	Goldman Sachs Asia, 14 Nov 2007.
	Jan 2008	5.2	--	--		--	--	--	Apple Daily, 26 Jan 2008.
Morgan Stanley Asia	Nov 2007	5.5	--	--		--	--	3	Morgan Stanley Asia, 13 Nov 2007.
	Feb 2008	5.5	--	--		--	--	4	Morgan Stanley Asia, 19 Feb 2008.
	May 2008	5.5	--	--		--	--	4.5	Morgan Stanley Asia, 14 May 2008.
JP Morgan Chase Bank	Feb 2008	5.3	--	--		--	--	3.5	JP Morgan Chase Bank 18 Feb 2008.
	May 2008	4.6	--	--		--	--	4.5	JP Morgan Chase Bank 13 May 2008.
Merrill Lynch	Oct 2007	6	6	7.7		--	--	2.8	Economics, Hong Kong, 22 Oct 2007.
	Feb 2008	6	--	--		--	--	3.9	The Asian Macro Weekly, 15 Feb 2008.
	May 2008	6	--	--		--	--	3.9	The Asian Macro Weekly, 9 May 2008.
Credit Suisse	Dec 2007	4.6	6.5	4.9		--	--	5.1	Emerging Markets Quarterly, 6 Dec 2007.
	Mar 2008	3.9	5.6	8.6		--	--	4.9	Emerging Markets Quarterly, 12 Mar 2008.

Table 3 (cont'd)

2008 GDP and price forecasts for Hong Kong put out by selected international organisations and private sector analysts

	Date of release	GDP (growth rate)	Private consumption expenditure rate	Gross domestic fixed capital formation		Total exports of goods terms	Exports of services (%)	Rate of change in consumer prices (%)	Reference source
				in	real				
Lehman Brothers	Dec 2007	5	--	--	--	--	--	3.4	HK Commercial Daily, 13 Dec 2007.
	Feb 2008	4.5	--	--	--	--	--	4.5	Global Weekly Economic Monitor, 15 Feb 2008.
	May 2008	4.3	--	--	--	--	--	5	Lehman Brothers, 13 May 2008.
<i>(c) Others</i>									
Economist Intelligence Unit	Jan 2008	4.8	7.4	6.5	--	--	--	3.9	Country Forecast, Jan 2008.
	Feb 2008	4	5.4	4.5	--	--	--	3.7	Country Forecast, Feb 2008.
	Mar 2008	4	5.1	4.5	--	--	--	4	Country Forecast, Mar 2008.
	Apr 2008	4.9	8	6.1	--	--	--	4.3	Country Forecast, Apr 2008.
Hong Kong General Chamber of Commerce	Nov 2007	5	--	--	--	--	--	3	HKGCC, 12 Nov 2007.
	Feb 2008	3.5	--	--	--	--	--	5	HKGCC, 20 Feb 2008.
Federation of Hong Kong Industries	Jan 2008	4.5	--	--	--	--	--	--	Press release, 10 Jan 2008.
University of Hong Kong	Jan 2008	5.6	--	--	--	--	--	--	Press release, 3 Jan 2008.

Observation :

The forecasts of GDP growth in real terms for 2008 from the private sector analysts listed above are mostly in the range of 4.5% to 5.5%, averaged at 4.9%.