

Press Release

(embargoed until 4:30 p.m. on 15 May 2009)

Economic Situation in the First Quarter of 2009 and Latest GDP and Price Forecasts for 2009

The Government released today (Friday) the First Quarter Economic Report 2009, together with the preliminary figures on Gross Domestic Product for the first quarter of 2009.

Details of the economic situation in the first quarter of 2009 and the latest GDP and price forecasts for the year are given below.

MAIN POINTS

- * The global financial crisis and the ensuing severe recession continued to weigh heavily on Hong Kong economy. Following a contraction of 2.6% in the fourth quarter of 2008, GDP registered a sharp year-on-year decline of 7.8% in real terms in the first quarter of 2009. This marked the largest decline since the third quarter of 1998 when the economy was severely battered by the Asian Financial Crisis.
- * On the trade front, Hong Kong's merchandise exports, like many other economies in the region, faced the double blow from sharp plunge in global demand and from an acute fall-off in intra-regional exports which were closely tied to demand in advanced economies. Total exports of goods plummeted by 22.7% in the first quarter over a year earlier, the largest decline since the second quarter of 1954. Exports of services declined by 8.2%, similarly hit by the plunge in global and regional demand. Inbound tourism nevertheless stood out as the bright spot with a further solid growth, thanks to the continued growth in Mainland visitors, partly helped by the further liberalisation measures under the Individual Visit Scheme.
- * In such a difficult and uncertain global economic climate, local sentiments were naturally depressed. In the first quarter of 2009, private consumption expenditure fell by 5.5% when set against the very high base of comparison in the same quarter of 2008. Yet the decline on a quarter-to-quarter basis actually tapered, and this reflected in part the relative improvements in the local stock and property markets during the quarter, and conceivably also the stimulus from the several rounds of packages announced since last year. Overall investment remained much in a sluggish state, down by 12.6% in the first quarter over a year earlier.
- * The labour market continued to adjust to the economic downturn through downsizing and wage cuts. The unemployment rate rose to 5.2% in the first quarter. As both local and external price pressures receded, consumer price inflation continued to trend down. The underlying inflation rate eased to 3.1% in

the first quarter, from 5.4% in the fourth quarter of 2008.

- * With the pace of deterioration in global demand markedly worse than earlier expectations thereby leading to the severe contraction in Hong Kong economy in the first quarter, and taking into account the considerable mark-down in world economic outlook since the Budget round, GDP for 2009 as a whole is now forecast to contract by 5.5-6.5% in real terms, down from the forecast decline of 2-3% put out in the Budget round.
- * Amid the difficult external environment, Hong Kong's exports of goods and services are likely to remain sluggish in the near term. Nevertheless, with the prospect of global contraction somewhat stabilising after the exceptional fall-offs earlier on, Hong Kong's external trade should see some relative improvement later in the year. More importantly, the Mainland economy is poised for a return to faster growth, with the massive stimulus measures successively in place and with both export orders and production activities concurrently reviving.
- * Domestically, consumer spending may remain moderate going forward, but the recent rebound in the local stock and housing markets, and the distinctly low interest rates, should hopefully render support to a relatively more stable local environment. Investment however is expected to remain depressed until the local economy shows clear signs of turnaround.
- * The latest GDP forecast is clearly subject to an unusually large degree of uncertainty from the still evolving global financial and economic environments. The outbreak of the human swine influenza in North America has also emerged as a new source of uncertainty for both the global and Hong Kong economy. Yet the expected pick-up in the Mainland economy, the recent rebound in global stock markets, the relative improvement in economic sentiment both in US and Europe, have provided glimpse of light at the end of a long tunnel, although a strong recovery is not yet in sight.
- * On inflation outlook, as an integral part of cost and price adjustments in economic downturn, price pressures from both the external and domestic fronts are rapidly receding and are expected to come down further in the months ahead. Factoring in the actual outturn in the first quarter, the forecast rate of increase in the headline Composite CPI for 2009 is marked down to 1% from 1.6% in the Budget round. The corresponding forecast underlying inflation rate is revised accordingly to 0.9%, from the earlier forecast of 1.5%.

DETAIL

GDP

According to the preliminary figure on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, GDP fell sharply by 7.8% in real terms in the first quarter of 2009 over a year earlier. Compared to the 2.6% decline in the fourth quarter, the marked deterioration in performance in the first quarter was due to an unprecedented fall-off in world trade as global recession plunged into the most severe recession since the World War II. On a seasonally adjusted quarter-to-quarter comparison, GDP fell by 4.3% in real terms in the first quarter of 2009, the fourth consecutive quarter of contraction (*Chart*).

2. The latest figures on GDP and its major expenditure components up to the first quarter of 2009 are presented in *Table 1*. Developments in different segments of the economy in the first quarter of 2009 are described below.

External trade

3. *Total exports of goods* plunged by 22.7% in real terms year-on-year in the first quarter of 2009, markedly down from the 4.9% decline in the fourth quarter of 2008. On a seasonally adjusted quarter-to-quarter comparison, total exports of goods fell sharply by 16.8% in real terms in the first quarter of 2009. Not only exports to the US and EU fell off markedly, so did exports to the Asian markets, as production activities along the supply chains in the region were cut back significantly in the face of the dwindling demand in the advanced economies. The sharp decline in Hong Kong's exports was thus part of a region-wide phenomenon amid the worst global recession in more than sixty years. In fact, in comparison, the extent of decline in exports in Hong Kong was similar to that in the Mainland, but less severe than in many other Asian economies.

4. *Exports of services* similarly slackened further in the first quarter, down by 8.2% year-on-year and 7.5% on a quarter-to-quarter seasonally adjusted basis. The collapse in world trade weighed heavily on exports of trade-related services (mainly offshore trade) as well as exports of transportation services. Exports of financial services and other business services were also much affected, as financial market and commercial activities were notably below the levels before the eruption of the financial tsunami last year. But inbound tourism stood out as a bright spot with a further solid growth, thanks to still rising Mainland visitors, partly supported by the further liberalisation measures under the Individual Visit Scheme.

Domestic sector

5. Domestic demand was also weak. *Private consumption expenditure (PCE)* fell by 5.5% in real terms year-on-year in the first quarter of 2009, upon higher unemployment and slackened income. But also relevant was a very high base of

comparison in the first quarter last year when consumption had an 8.0% growth. In fact, on a seasonally adjusted quarter-to-quarter basis, the decline in consumption tapered to 1.5%, as consumer sentiment was supported to some extent by the stabilisation in the local stock and property markets in the quarter as well as by the relief measures put out by the Government over the past year or so.

6. *Overall investment spending* remained much in a depressed mode, down by 12.6% in the first quarter over a year earlier. Machinery and equipment investment was held back by the grim economic outlook. The results of latest Quarterly Business Tendency Survey conducted by the Census and Statistics Department in March and early April indicated that large companies remained rather pessimistic about the near-term business situation, but the extent of pessimism seemed to have lessened somewhat compared with the survey results obtained three months earlier. Expenditure on building and construction also fell notably in the first quarter, mainly due to a steep decline in private sector construction activity. Nevertheless, the efforts to accelerate public sector projects should begin to pay off in the coming quarters.

The labour sector

7. Labour market conditions continued to worsen in face of the economic contraction. The seasonally adjusted *unemployment rate* rose to 5.2% in the first quarter as business downsizing intensified both in terms of scale and pace under the heavy influence of the deepening global recession. The *underemployment rate* also rose, to 2.1%. There were also greater downward pressures on wages and earnings.

Prices

8. Inflationary pressure eased notably further in the first quarter on the back of receding local and external price pressures. *Underlying consumer price inflation* came down to 3.1% in the first quarter, mostly helped by the lower food price inflation and recent easing in private housing rentals. *Headline consumer price inflation*, being affected by the relevant one-off relief measures, was lower at 1.7%, due mainly to the electricity subsidy that began to take effect since September last year. As to the *GDP deflator*, an increase of 0.5% was recorded in the first quarter, due to a more favourable terms of trade offsetting the decline in domestic demand deflator.

Latest GDP and price forecasts for 2009

9. According to the International Monetary Fund (IMF), world GDP would contract by 1.3% in 2009, representing the most severe recession during the post-war period. Even granting that governments of major economies would step up efforts to heal the financial sector while continuing to support demand through monetary and fiscal easing, IMF believed that a slow recovery would only begin to take hold in 2010. Against this background, the external environment will remain difficult and challenging in the rest of 2009.

10. Nevertheless, there are some early signs suggesting that the rate of economic contraction in the United States, the epicentre of the global financial crisis, will slow in the coming quarters. More importantly, the Mainland economy is set to return to a faster growth path, as the massive stimulus measures are successively in place and as export orders and production activities are also reviving concurrently. Thus, while Hong Kong's exports are likely to remain sluggish in the near term, it should post some relative improvement later this year.

11. Domestically, consumer spending may remain moderate going forward, but the recent rebound in the local stock and housing markets, and the distinctly low interest rates, should hopefully render support to a relatively more stable local environment. Investment however is expected to remain depressed until the local economy shows clear signs of turnaround.

12. With the pace of deterioration in global demand markedly worse than earlier expectations thereby leading to the severe contraction in Hong Kong economy in the first quarter, and taking into account the considerable mark-down in world economic outlook since the Budget round, GDP for 2009 as a whole is now forecast to contract by 5.5-6.5% in real terms, down from the forecast decline of 2-3% put out in the Budget round (*Table 2*). By comparison, most private sector analysts are currently projecting the economy to contract by 2-5%, averaging at around -3.5%.

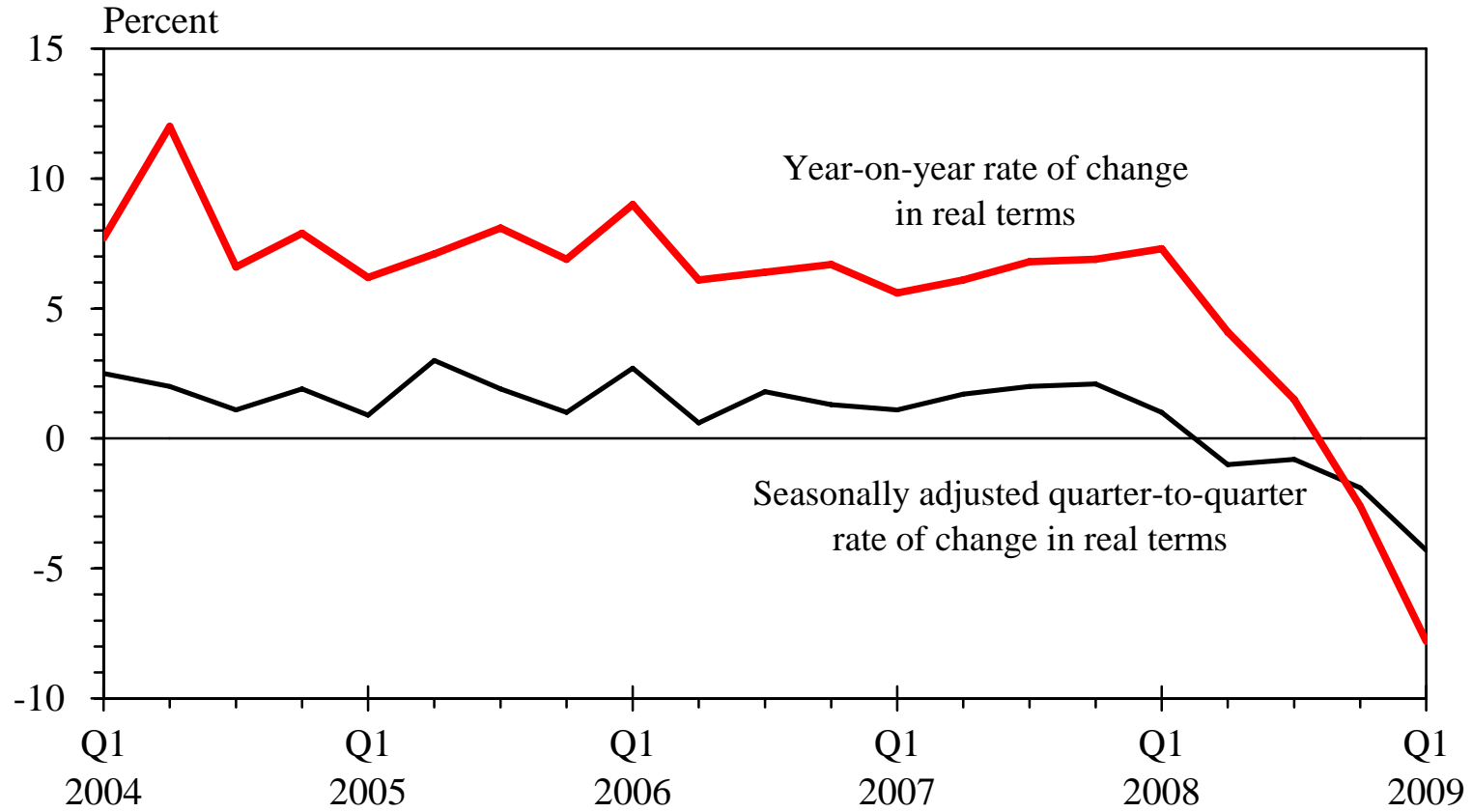
13. The latest GDP forecast is clearly subject to an unusually large degree of uncertainty from the still evolving global financial and economic environments. The outbreak of the human swine influenza in North America has also emerged as a new source of uncertainty for both the global and Hong Kong economy. Yet the expected pick-up in the Mainland economy, the recent rebound in global stock markets, the relative improvement in economic sentiment both in US and Europe, have provided glimpse of light at the end of a long tunnel, although a strong recovery may not come about any time soon.

14. On inflation outlook, as an integral part of cost and price adjustments in economic downturn, price pressures from both the external and domestic fronts are rapidly receding and are expected to come down further in the months ahead. Factoring in the actual outturn in the first quarter, the forecast rate of increase in the headline Composite CPI for 2009 is marked down to 1%, from 1.6% in the Budget round. The corresponding forecast underlying inflation rate is revised accordingly to 0.9%, from the earlier forecast of 1.5%.

(The First Quarter Economic Report 2009 is now available for online download, free of charge at <http://www.hkeconomy.gov.hk/en/reports/index.htm>. The Report of the Gross Domestic Product, First Quarter 2009, which contains the GDP figures up

to the first quarter of 2009, is also available for online download, free of charge at the homepage of the Census and Statistics Department (<http://www.censtatd.gov.hk>). Users can purchase the print version of these two publications online at the Government Bookstore at <http://www.bookstore.gov.hk>, or by calling the Publications Sales Unit of the Information Services Department at 2537 1910. The print version of the two reports is available for sale at \$60 and \$49 per issue respectively, plus postage charge.)

Hong Kong's Gross Domestic Product



Note : Figures for the first quarter of 2009 are preliminary estimates.

Table 1

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

	<u>2007#</u>	<u>2008#</u>	<u>Q1#</u>	<u>Q2#</u>	<u>2008</u> <u>Q3#</u>	<u>Q4#</u>	<u>2009</u> <u>Q1+</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>							
Private consumption expenditure	8.5	1.5	8.0 (*)	3.0 (-1.3)	-0.2 (-0.6)	-4.1 (-2.2)	-5.5 (-1.5)
Government consumption expenditure	3.0	1.7	0.6 (-0.3)	3.1 (1.6)	1.6 (-0.5)	1.8 (0.8)	1.5 (-0.3)
Gross domestic fixed capital formation	3.4	-0.5	9.9	5.1	2.9	-17.8	-12.6
<i>of which :</i>							
Building and construction	-0.3	1.6	9.1	-0.1	-2.8	0.1	-8.2
Machinery, equipment and computer software	3.0	-0.3	4.3	7.4	10.7	-21.1	-6.6
Total exports of goods	7.0	1.9	8.3 (0.9)	4.4 (0.1)	1.3 (-1.8)	-4.9 (-4.3)	-22.7 (-16.8)
Imports of goods	8.8	1.8	8.4 (-1.7)	4.8 (1.9)	2.0 (-1.2)	-6.4 (-5.6)	-21.4 (-15.9)
Exports of services	14.1	5.7	10.1 (1.5)	8.4 (0.3)	4.8 (0.1)	0.4 (-1.3)	-8.2 (-7.5)
Imports of services	12.1	3.3	11.2 (1.3)	3.8 (-2.6)	2.2 (-0.1)	-3.4 (-1.8)	-10.9 (-6.8)
Gross Domestic Product	6.4	2.4	7.3 (1.0)	4.1 (-1.0)	1.5 (-0.8)	-2.6 (-1.9)	-7.8 (-4.3)
<i>Change in the main price indicators (%)</i>							
GDP deflator	2.9	1.4	2.3 (-1.5)	1.9 (0.6)	2.0 (0.9)	-0.2 (-0.2)	0.5 (-0.7)
Composite CPI							
Headline	2.0	4.3	4.6 (0.9)	5.7 (1.5)	4.6 (-0.2)	2.3 (0.1)	1.7 (0.3)
Underlying^	2.8	5.6	4.9 (2.0)	5.7 (1.5)	6.3 (1.3)	5.4 (0.4)	3.1 (-0.2)
Change in nominal GDP (%)	9.5	3.8	9.7	6.1	3.5	-2.8	-7.3

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%.

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

Table 2

**Economic forecasts for 2009
(year-on-year rate of change (%))**

	Forecasts for 2009 as released <u>on 25.2.2009</u> (%)	Latest forecasts for 2009 <u>on 15.5.2009</u> (%)
Gross Domestic Product (GDP)		
<i>Real GDP</i>	-2 to -3	-5.5 to -6.5
<i>Nominal GDP</i>	-1.5 to -2.5	-5.5 to -6.5
Composite Consumer Price Index (CCPI)		
<i>Headline CCPI</i>	1.6	1
<i>Underlying CCPI</i>	1.5	0.9
GDP Deflator	0.5	0