

Press Release

(embargoed until 4:30 p.m. on 13 November 2009)

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

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

The Government Economist, Mrs Helen Chan, described the economic situation in the third quarter of 2009 and provided the latest GDP and price forecasts for the year.

MAIN POINTS

- * The Hong Kong economy improved further after a strong rebound during the second quarter, leading to a further tapering of the year-on-year decline in real GDP to 2.4% in the third quarter. This was led mainly by the further improvement in the domestic sector, offsetting the drag from the weak external demand. On a seasonally adjusted quarter-to-quarter comparison, real GDP expanded further by 0.4% in the third quarter over the second quarter.
- * Although the global economy had entered the initial stage of recovery, import demand in the advanced economies remained sluggish and continued to weigh heavily on exports of Asian economies. Against this backdrop, Hong Kong's merchandise exports still declined notably year-on-year in the third quarter, although the pace of decline slowed distinctly towards the end of the quarter.
- * In contrast, exports of services improved more visibly in the third quarter, supported by further revival in financial market activities and a rebound in inbound tourism. Yet trade-related service exports were still weak under the drag of sluggish trade flows.
- * Local consumer sentiments revived further in the third quarter, as economic prospects got better, the labour market stabilized, Government's relief measures yielded further results, and asset markets remained supportive. Private consumption expenditure, having fallen for four consecutive quarters, bottomed out in the third quarter on a year-on-year basis. Business sentiments turned up distinctly, with overall investment reverting to a small increase after three consecutive quarters of double-digit decline.
- * Labour market showed initial signs of improvement after a period of successive worsening since late 2008. The seasonally adjusted unemployment rate fell slightly to 5.3% in the third quarter, the first decline since the onset of the global financial crisis.

- * Following the exceptionally large stimulus measures by governments and central banks to shore up demand and stabilize the financial markets, the global economy is finally expanding again. Despite this, labour markets in many advanced economies continued to worsen. These economies are still confronted by impaired financial systems and an on-going adjustment process to deleverage and rebuild savings. Yet in Asia, the improvement has been more evident, with the Mainland economy taking the lead in the return to a faster growth path. With global trade flows still notably down as compared to the pre-crisis level, there are indications that orders are gradually coming back in recent months and the onset of a modest global recovery and the restocking process should help Hong Kong's external trade going forward.
- * Domestically, local consumer sentiments should continue to be supported by an improving labour market and the cushion rendered by the Government's relief measures. As for businesses, the results of latest Quarterly Business Tendency Survey conducted by the Census and Statistics Department in September and early October indicated that many large business establishments have turned more upbeat about their near-term business prospects. Also, public sector investment should continue apace to shore up aggregate demand, as part of the Government's counter-cyclical strategy in the current global downturn.
- * With both domestic and external sectors likely to show further improvement in the fourth quarter, and taking into account the actual outturn so far, GDP for 2009 as a whole is now forecast to contract by 3.3% in real terms, up from the forecast decline of 3.5-4.5% in the August round.
- * Although the downside risks in the external environment seem to have receded for the time being, the global economic outlook in the period ahead remains subject to considerable uncertainties. The clear risk is that the global recovery could stall after the exceptionally fiscal boost begins to fade out. The "toxic assets" in the US and European financial systems and the deleveraging process to restore health in the banking sector are the key drags to the recovery process. Another major risk is the timing and pace of the exit strategies by governments and central banks, and the possible fluctuations in the asset markets they may cause. The potential rise in protectionist sentiment is another concern.
- * On inflation outlook, both local and external price pressures are virtually absent, as local costs remain contained and as the supply capacity of the global economy still out-runs demand by a sizable margin. Underlying Composite CPI went lower by 0.3% in the third quarter from a year earlier, but the underlying deflationary pressure had tended to stabilise towards the end of the quarter on a seasonally adjusted basis. Hence, the deflationary pressure facing the economy has been relatively contained thus far. With the development on the price front largely in line with the earlier expectations, the forecast headline and underlying consumer price inflation rates remain unchanged, at 0.5% and 0.9% respectively for 2009 as a whole.

DETAIL

GDP

According to the preliminary figure on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, real GDP registered a decline of 2.4% in the third quarter over a year earlier. The decline was narrower than the 3.6% (revised upwards from an earlier estimate of -3.8%) decline in the second quarter. On a seasonally adjusted quarter-to-quarter comparison, GDP expanded by 0.4% in real terms in the third quarter (*Chart*).

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

External trade

3. *Total exports of goods* continued to fall notably by 13.2% in real terms year-on-year in the third quarter of 2009, following the decline of 12.4% in the preceding quarter. On a seasonally adjusted quarter-to-quarter comparison, total exports of goods dipped by 2.8% in the third quarter after an exceptionally strong rebound of 11.6% in the previous quarter. With global trade flows still languishing at a relatively low level, many other Asian economies continued to record double-digit declines in exports in the quarter. Yet the pace of decline in Hong Kong's merchandise exports slowed distinctly towards the end of the quarter.

4. *Exports of services* showed visible improvement in the third quarter of 2009. On a seasonally adjusted quarter-to-quarter basis, exports of services expanded rapidly by 4.6% in the third quarter, leading to a distinct tapering in the year-on-year rate of decline to just 0.9%, from that of 5.2% in the second quarter. Exports of financial services continued to improve alongside the further revival in financial market activities. Exports of travel services likewise reverted to an increase, in tandem with a rebound in visitor arrivals. Yet exports of transportation services and trade-related services were still weak, under the drag of the much slackened trade flows in goods.

Domestic sector

5. Local consumer sentiments revived further in the third quarter, riding on a generally improved labour market, and Government's several rounds of relief measures, and further aided by favourable asset market conditions. *Private consumption expenditure (PCE)* expanded further by 0.5% in real terms in the third quarter on a seasonally adjusted quarter-to-quarter basis after a strong rebound in the second quarter. The year-on-year change also reversed back to a small increase of 0.2%, after falling for four consecutive quarters.

6. Business sentiments turned up distinctly in the third quarter. *Overall investment spending* returned to a small growth of 1.4% in the third quarter over a year earlier. Yet this represented a distinct improvement from the 13.6% decline in the second quarter. Expenditure on building and construction rose by 3.4% in the third quarter, arresting the decline of 4.7% in the second quarter. The growth in public sector construction work accelerated significantly further amidst the Government's efforts to expedite public sector projects, while private sector construction work also saw a further relative improvement. The year-on-year decline in machinery and equipment investment also eased notably to 4.0% in the third quarter from the 18.0% decline in the second quarter.

The labour sector

7. Labour market showed initial signs of improvement, after a period of successive worsening since late 2008. In the third quarter, the seasonally adjusted *unemployment rate* fell slightly to 5.3%, the first decline since the onset of the global financial crisis in September 2008. The *underemployment rate* registered only a slight increase by 0.1 percentage point to 2.4%, with its movement holding broadly stable in recent months. Meanwhile, earnings and wages remained on a decline in the second quarter.

Prices

8. Inflationary pressure has basically subsided, as local business costs were contained and import prices softened in the aftermath of the global financial tsunami. *Underlying consumer price inflation* turned slightly negative at -0.3% in the third quarter, while *headline consumer price inflation*, being kept down by the one-off measures (mainly the electricity subsidy in July and August), went even lower to -0.9%. Nevertheless, on a seasonally adjusted basis, the underlying deflationary pressure had tended to stabilise towards the end of the quarter. As to the *GDP deflator*, a slight increase of 0.4% was recorded in the third quarter, as the deflator for machinery and equipment increased notably and the terms of trade rose marginally.

Latest GDP and price forecasts for 2009

9. Following the exceptionally large stimulus measures by governments and central banks to shore up demand and stabilize the financial markets, the global economy is finally expanding again. Despite this, labour markets in many advanced economies continued to worsen. These economies are still confronted by impaired financial systems and an on-going adjustment process to deleverage and rebuild savings. Yet in Asia, the improvement has been more evident, with the Mainland economy taking the lead in the return to a faster growth path. With global trade flows still notably down as compared to the pre-crisis level, there are indications that orders are gradually coming back in recent months and the onset of a modest global recovery and the restocking process should help Hong Kong's external trade going forward.

10. Domestically, local consumer sentiments should continue to be supported by an improving labour market and the cushion rendered by the Government's relief measures. As for businesses, the results of latest Quarterly Business Tendency Survey conducted by the Census and Statistics Department in September and early October indicated that many large business establishments have turned more upbeat about their near-term business prospects. Also, public sector investment should continue apace to shore up aggregate demand, as part of the Government's counter-cyclical strategy in the current global downturn.

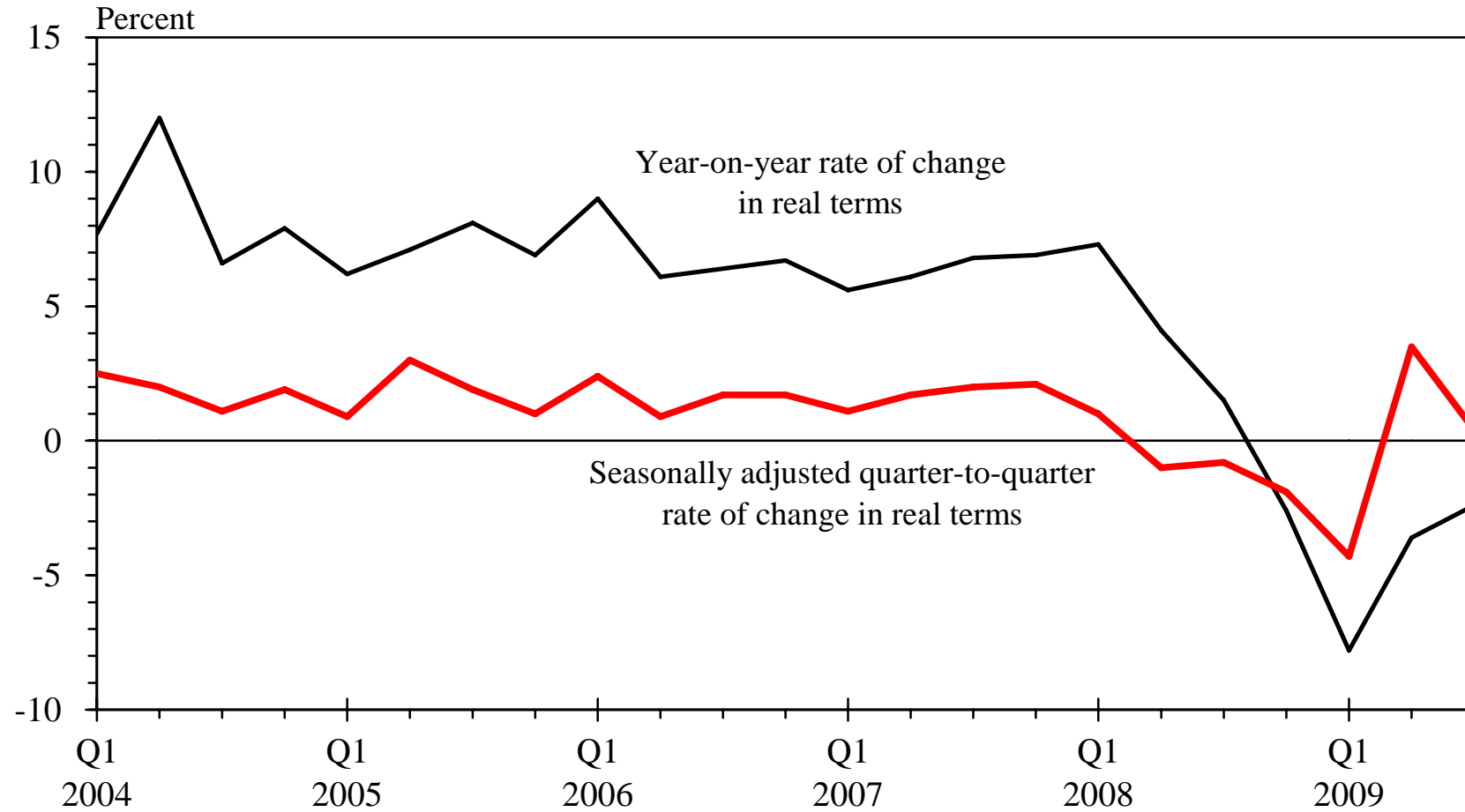
11. With both domestic and external sectors likely to show further improvement in the fourth quarter, and taking into account the actual outturn so far, GDP for 2009 as a whole is now forecast to contract by 3.3% in real terms, up from the forecast decline of 3.5-4.5% in the August round (*Table 2*). By comparison, most private sector analysts are currently projecting the economy to contract by 2.5-5.0%, averaging at around -3.6%.

12. Although the downside risks in the external environment seem to have receded for the time being, the global economic outlook in the period ahead remains subject to considerable uncertainties. The clear risk is that the global recovery could stall after the exceptionally fiscal boost begins to fade out. The "toxic assets" in the US and European financial systems and the deleveraging process to restore health in the banking sector are the key drags to the recovery process. Another major risk is the timing and pace of the exit strategies by governments and central banks, and the possible fluctuations in the asset markets they may cause. The potential rise in protectionist sentiment is another concern.

13. On inflation outlook, both local and external price pressures are virtually absent, as local costs remain contained and as the supply capacity of the global economy still out-runs demand by a sizable margin. Nevertheless, the underlying deflationary pressure had tended to stabilise towards the end of the quarter on a seasonally adjusted basis, and hence the deflationary pressure facing the economy has been relatively contained thus far. With the development on the price front largely in line with the earlier expectations, the forecast headline and underlying consumer price inflation rates remain unchanged, at 0.5% and 0.9% respectively for 2009 as a whole.

(The Third 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, Third Quarter 2009, which contains the GDP figures up to the third 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 \$90 and \$49 per issue respectively, plus postage charge.)

Hong Kong's Gross Domestic Product



Note : Figures for the third 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>2008</u>				<u>2009</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	8.5	1.5	8.0 (*)	3.0 (-1.3)	-0.2 (-0.6)	-4.1 (-2.2)	-6.0 (-2.0)	-1.1 (3.9)	0.2 (0.5)
Government consumption expenditure	3.0	1.7	0.6 (-0.3)	3.1 (1.6)	1.6 (-0.5)	1.8 (0.8)	1.4 (-0.3)	1.7 (1.6)	3.3 (1.3)
Gross domestic fixed capital formation	3.4	-0.5	9.9	5.1	2.9	-17.8	-13.7	-13.6	1.4
<i>of which :</i>									
Building and construction	-0.3	1.6	9.1	-0.1	-2.8	0.1	-10.9	-4.7	3.4
Machinery, equipment and computer software	3.0	-0.3	4.3	7.4	10.7	-21.1	-6.6	-18.0	-4.0
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)	-12.4 (11.6)	-13.2 (-2.8)
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)	-12.7 (10.9)	-8.3 (3.6)
Exports of services	14.1	5.7	10.1 (1.5)	8.4 (0.3)	4.8 (0.1)	0.4 (-1.3)	-6.3 (-5.6)	-5.2 (1.7)	-0.9 (4.6)
Imports of services	12.1	3.3	11.2 (1.3)	3.8 (-2.6)	2.2 (-0.1)	-3.4 (-1.8)	-9.6 (-5.5)	-5.6 (1.8)	-3.8 (1.9)
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)	-3.6 (3.5)	-2.4 (0.4)
<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)	0.4 (-0.8)	1.1 (1.3)	0.4 (0.1)
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)	-0.1 (-0.2)	-0.9 (-1.1)
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)	1.2 (-0.3)	-0.3 (-0.1)
<u>Change in nominal GDP (%)</u>	9.5	3.8	9.7	6.1	3.5	-2.8	-7.4	-2.5	-2.0

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
(rate of change (%))**

	Forecasts for 2009 as released <u>on 14.8.2009</u> (%)	Latest forecasts for 2009 <u>on 13.11.2009</u> (%)
Gross Domestic Product (GDP)		
<i>Real GDP</i>	-3.5 to -4.5	-3.3
<i>Nominal GDP</i>	-3.5 to -4.5	-2.8
Composite Consumer Price Index (CCPI)		
<i>Headline CCPI</i>	0.5	0.5
<i>Underlying CCPI</i>	0.9	0.9
GDP Deflator	0	0.5