

Press Release

(embargoed until 4:30 p.m. on 13 May 2011)

Economic Situation in the First Quarter of 2011 and Latest GDP and Price Forecasts for 2011

The Government released today (Friday) the First Quarter Economic Report 2011, together with the preliminary figures on Gross Domestic Product for the first quarter of 2011.

The Government Economist, Mrs Helen Chan, described the economic situation in the first quarter of 2011 and provided the latest GDP and price forecasts for the year.

MAIN POINTS

- * The Hong Kong economy sustained strong momentum in the first quarter of 2011, with real GDP leaping by 7.2% over a year earlier. Growth in the first quarter was slightly higher than the already appreciable 7.0% growth for 2010 as a whole, marking the fifth consecutive quarter that growth was distinctly above the average annual growth over the past 10 years. On a seasonally adjusted quarter-to-quarter comparison, GDP grew notably by 2.8% in real terms in the first quarter.
- * Merchandise exports resumed the strong uptrend in the first quarter, surging by 16.8% in real terms over a year earlier. This was attributable to the strong growth of the Mainland economy spurring production and export activities in the Asian region as a whole. The US and European markets also grew further, albeit still lagging far behind the Asian markets.
- * Exports of services likewise stayed buoyant in the first quarter, leaping by 9.1% in real terms over a year earlier, with particularly spectacular performance in exports of financial and business services. Exports of trade-related services and travel services both remained vibrant. Yet those of transportation services fared a bit less well and saw only modest growth.
- * On the domestic front, private consumption expenditure grew strongly in the first quarter, by 7.6% in real terms over a year earlier, on the back of improving job and income situations. The large-scale infrastructure projects under way lent further support to domestic demand. Yet machinery and equipment investment, which is usually rather volatile, reverted to a decline, thereby resulting in a modest 1.1% fall-back in overall investment spending in the first quarter. Nevertheless, local business confidence remained sanguine during the first quarter.
- * The labour market saw further broad-based improvement. Job creation gathered pace in tandem with the strong economic expansion. The seasonally adjusted unemployment rate came down progressively to 3.4% in the first quarter, largely back to the post-1997 low of 3.3% in mid-2008. Labour wages and earnings continued to increase. The median household income rose by

5.6% in the first quarter in nominal terms over a year earlier, or by 1.7% in real terms after discounting inflation. Over the same period, average employment earnings for the lowest decile of full-time employees rose by 6.2% in nominal terms or by 2.0% in real terms.

- * Overall residential flat prices rose by 9% during the first quarter, surpassing the peak in 1997. The Government has recently introduced further initiatives to increase land supply. The Hong Kong Monetary Authority has stepped up examinations on banks' mortgage business. The Government will monitor the housing market situation closely to ensure its stable and healthy development.
- * The external environment has held up well so far this year. The global economy has continued to expand, led by the thriving Asian and emerging economies. Economic recovery in the US and Europe, while still sluggish, has gradually been on firmer footing. Yet uncertainties in the external environment still abound. While old factors, such as the sovereign debt problem in the eurozone, have yet to be resolved, new uncertainties have emerged, including further macroeconomic policy tightening in Asia, political unrest in the Middle East and North Africa, and potential disruption to the regional supply chain due to Japan's earthquake and nuclear incident. These old and new uncertainties would pose some downside risks to Hong Kong's external trade, possibly causing export growth to slow in the coming quarters.
- * The domestic sector should stay rather robust. Local consumption should continue to be well supported by improving job and income conditions. As for business confidence, the results of the latest Quarterly Business Tendency Survey showed that large enterprises remained positive on the near-term business outlook. In addition, the expected pick-up in infrastructure works should render further impetus to domestic demand.
- * With real GDP churning out a stronger-than-expected 7.2% year-on-year growth in the first quarter, and even allowing for some moderation in the rest of the year, the economy is poised for a real growth of 5-6% for 2011 as a whole, revised upwards by 1 percentage point from the 4-5% forecast announced in February.
- * Underlying consumer price inflation (by reference to the 2009/10-based series), which nets out the effect of the Government's relief measures to reflect the inflation trend more accurately, rose to 3.7% in the first quarter from 2.4% in the fourth quarter of last year. The further increase in price pressure lately was the combined results of rising imported inflation and local costs. On the external front, global commodity prices soared on the back of a weak US dollar, the global liquidity glut, and strong demand from emerging economies, with particularly notable surge in food prices. Political unrest in the Middle East and North Africa has added further upward pressure on the already elevated oil prices and worldwide inflation. Indeed, inflation has become a common challenge faced by Asian economies with vibrant growth.
- * Domestically, upward pressures on local costs have increased after five quarters

of very rapid economic growth. The feed-through of the surge in housing rentals last year to the consumer price level is expected to become more visible in the coming months. With the economy near full employment plus the one-off effect from the implementation of Statutory Minimum Wage, upward pressures on local wages are likely to rise further. With domestic and external factors both adding to local inflation in the near term, the forecast rates of headline and underlying consumer price inflation for 2011 as a whole (by reference to the 2009/10-based series) are revised upwards to 5.4% and 5.5% respectively, from the 4.5% first announced in the Budget in February this year.

DETAILS

GDP

According to preliminary data on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, real GDP leaped by 7.2% in the first quarter of 2011 over a year earlier, slightly higher than the already strong 7.0% growth for 2010 as a whole (revised upwards from the preliminary estimate of 6.8%). On a seasonally adjusted quarter-to-quarter comparison, real GDP grew by 2.8% in the first quarter, the eighth consecutive quarter of expansion (*Chart*).

2. The latest figures on GDP and its major expenditure components up to the first quarter of 2011 are presented in *Table 1*. Developments in different segments of the economy in the first quarter of 2011 are described below.

External trade

3. *Total exports of goods* surged by 16.8% in real terms in the first quarter of 2011 over a year earlier, re-accelerating from the 8.2% growth in the fourth quarter of 2010. On a seasonally adjusted quarter-to-quarter basis, total exports of goods also gathered steam and leaped by 14.4% in real terms over the preceding quarter. The strong export performance was driven mainly by the robust growth of the Asian markets, particularly the Mainland. Exports to the US and Europe grew further, albeit still lagging behind other major markets, and also yet to bounce back to the pre-crisis levels.

4. *Exports of services* grew briskly by 9.1% year-on-year in real terms in the first quarter of 2011, following the 9.3% growth in the fourth quarter of 2010. On a seasonally adjusted quarter-to-quarter comparison, exports of services grew further by 4.0% in real terms in the first quarter. Exports of financial and other business services surged on the back of strong growth in cross-border financing and sustained external demand for Hong Kong's commercial and professional services. Exports of trade-related services grew robustly further in tandem with vibrant regional trade flows. Exports of travel services likewise grew apace, thanks to strong tourist arrivals from Asia as a whole and further increase in arrivals from the long-haul markets. Yet exports of transportation services recorded only moderate growth.

Domestic sector

5. Domestically, *private consumption expenditure* grew strongly further in the first quarter, by 7.6% in real terms over a year earlier. Consumer sentiment was well supported by the improving job and income situations and to some extent by the further increases in asset prices. On a seasonally adjusted quarter-to-quarter comparison, private consumption expenditure grew further by 0.7% in real terms in the first quarter. *Government consumption expenditure* continued to increase steadily in the first quarter, by 2.7% in real terms over a year earlier.

6. *Overall investment spending* however relapsed to a year-on-year decline of 1.1% in real terms in the first quarter. This was due to the fall-back in private machinery and equipment investment in the first quarter, by 13.8% in real terms, following a notable increase in 2010. On the other hand, building and construction expenditure in the public sector continued to surge. As such, overall building and construction expenditure still showed a notable growth of 13.4% in real terms, despite a further decline in private sector building and construction expenditure. The fall-off in overall investment in the first quarter was thus more likely to be a temporary aberration from the underlying uptrend.

The labour sector

7. The labour market saw further broad-based improvement in the first quarter of 2011 amid the robust economic conditions. The *seasonally adjusted unemployment rate* came down progressively to 3.4% in the first quarter, largely back to the post-1997 low of 3.3% in mid-2008. The *underemployment rate* also stayed low at 1.8%. Vacancies continued to surge, accompanied by further rise in labour wages and earnings. The median household income rose in the first quarter by 5.6% in nominal terms over a year earlier, or by 1.7% in real terms after discounting inflation. Over the same period, average employment earnings for the lowest decile of full-time employees rose by 6.2% in nominal terms or by 2.0% in real terms.

The asset markets

8. The *local stock market* went up slightly during the first quarter, amid some fluctuations due to the political unrest in the Middle East and North Africa and the earthquake in Japan. The Hang Seng Index closed the quarter at 23 528, 2% higher than at end-2010.

9. The *residential property market* saw a brief relapse towards the end of 2010 immediately after the Government's announcement of the Special Stamp Duty. Yet residential property prices rose back by 9% during the first quarter of 2011. By March 2011, overall flat prices had surpassed the historic peak in 1997 by around 3%. Residential property rentals showed a brief decline in January 2011, but resumed some increase in February and March, yet cumulating to an increase of

merely 1% between December 2010 and March 2011. Over the same period, rentals for offices and shops went up slightly by 2% and 1% respectively.

Prices

10. Consumer price inflation went up further during the first quarter. On the back of a more solid global recovery, loose monetary environment and a weaker US dollar, global commodity prices continued to surge, thereby leading to a notable increase in import prices. The political unrest in the Middle East and North Africa also fuelled the increase in oil prices. Meanwhile, domestic factors also played an increasing role in driving inflation amid the robust local economic conditions. This was particularly so on the rental front. In addition, with unemployment rate trending down to a level close to its post-1997 low, coupled with the implementation of Statutory Minimum Wage in May, wage pressures may become increasingly evident in the coming months. By reference to the new 2009/10-based series, *headline consumer price inflation* rose to 3.8% in the first quarter, from 2.7% in the fourth quarter of 2010 (or from 2.8% to 4.0% by reference to the old 2004/05-based series). Netting out the effect of the Government's relief measures, *underlying consumer price inflation* climbed up to 3.7% in the first quarter from 2.4% in the previous quarter (or from 2.6% to 3.9% by reference to the old 2004/05-based series).

11. The pick-up in underlying consumer price inflation in the first quarter was mainly driven by the further increases in food prices and housing costs. The former was due to the sustained and notable rise in imported food prices, and also to the greater pricing power of retailers and suppliers amid a buoyant consumption market. Higher private housing rentals in the CPI reflected the lagged feed-through of the strong rebound in market rentals since early 2009. Indeed, the increases in prices of the food and housing components accounted for more than 70% of the underlying inflation rate in the first quarter.

Latest GDP and price forecasts for 2011

12. The external environment has held up well so far this year. The global economy has continued to expand, led by the thriving Asian and emerging economies. Economic recovery in the US and Europe, while still sluggish, has gradually been on firmer footing. Yet uncertainties in the external environment still abound. While old factors, such as the sovereign debt problem in the eurozone, have yet to be resolved, new uncertainties have emerged, including further macroeconomic policy tightening in Asia, political unrest in the Middle East and North Africa, and potential disruption to the regional supply chain due to Japan's earthquake and nuclear incident. These old and new uncertainties would pose some downside risks to Hong Kong's external trade, possibly causing export growth to slow in the coming quarters.

13. The domestic sector should stay rather robust. Local consumption should continue to be well supported by improving job and income conditions. As

for business confidence, the results of the latest Quarterly Business Tendency Survey showed that large enterprises remained positive on the near-term business outlook. In addition, the expected pick-up in infrastructure works should render further impetus to domestic demand.

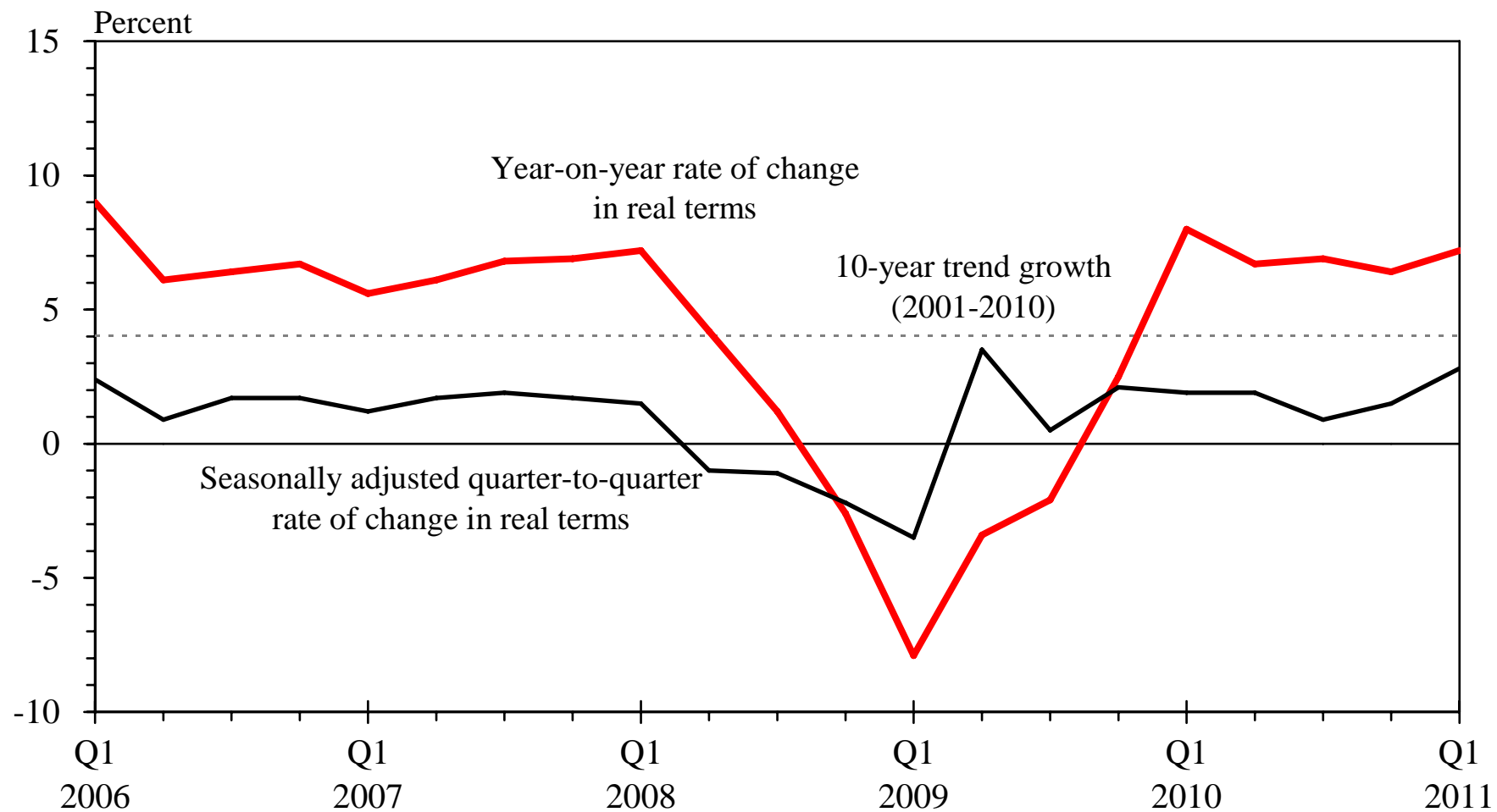
14. With real GDP churning out a stronger-than-expected 7.2% year-on-year growth in the first quarter, and even allowing for some moderation in the rest of the year, the economy is poised for a real growth of 5-6% for 2011 as a whole, revised upwards by 1 percentage point from the 4-5% forecast announced in February (*Table 2*). For information, most private sector analysts are currently projecting the economy to expand by 4.5-6%, averaging at around 5.2%.

15. Underlying consumer price inflation (by reference to the 2009/10-based series), which nets out the effect of the Government's relief measures to reflect the inflation trend more accurately, rose to 3.7% in the first quarter from 2.4% in the fourth quarter of last year. The further increase in price pressure lately was the combined results of rising imported inflation and local costs. On the external front, global commodity prices soared on the back of a weak US dollar, the global liquidity glut, and strong demand from emerging economies, with particularly notable surge in food prices. Political unrest in the Middle East and North Africa has added further upward pressure on the already elevated oil prices and worldwide inflation. Indeed, inflation has become a common challenge faced by Asian economies with vibrant growth.

16. Domestically, upward pressures on local costs have increased after five quarters of very rapid economic growth. The feed-through of the surge in housing rentals last year to the consumer price level is expected to become more visible in the coming months. With the economy near full employment plus the one-off effect from the implementation of Statutory Minimum Wage, upward pressures on local wages are likely to rise further. With domestic and external factors both adding to local inflation in the near term, the forecast rates of headline and underlying consumer price inflation for 2011 as a whole (by reference to the 2009/10-based series) are revised upwards to 5.4% and 5.5% respectively, from the 4.5% first announced in the Budget in February this year.

(The First Quarter Economic Report 2011 is now available for online download, free of charge at <http://www.hkeconomy.gov.hk/en/reports/index.htm>. The print version is available for sale at \$106 per issue, plus postage charge. Users can purchase the print version 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 Report of the Gross Domestic Product, First Quarter 2011, which contains the GDP figures up to the first quarter of 2011, is also available for online download, free of charge at the homepage of the Census and Statistics Department, <http://www.censtatd.gov.hk>.)

Hong Kong's Gross Domestic Product



Note : Figures for the first quarter of 2011 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>2009[#]</u>	<u>2010[#]</u>	<u>2010</u>				<u>2011</u>
			<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1⁺</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>							
Private consumption expenditure	0.7	6.2	7.4 (0.7)	4.1 (1.3)	5.3 (1.8)	8.1 (3.7)	7.6 (0.7)
Government consumption expenditure	2.3	2.7	3.3 (0.9)	2.7 (0.8)	3.2 (0.9)	1.6 (-0.8)	2.7 (1.9)
Gross domestic fixed capital formation	-3.9	7.8	8.2	15.8	-0.3	8.6	-1.1
<i>of which :</i>							
Building and construction	-5.5	6.6	-7.1	13.2	9.6	11.3	13.4
Machinery, equipment and computer software	-3.0	5.9	11.5	15.9	-7.3	6.4	-11.8
Total exports of goods	-12.7	17.3	21.6 (6.2)	20.2 (3.9)	20.8 (1.8)	8.2 (-3.5)	16.8 (14.4)
Imports of goods	-9.5	18.1	28.3 (7.5)	23.4 (3.3)	16.7 (-0.6)	7.5 (-2.3)	12.6 (12.0)
Exports of services	0.3	15.0	18.4 (4.1)	17.5 (2.2)	15.8 (2.2)	9.3 (0.3)	9.1 (4.0)
Imports of services	-4.9	10.4	11.2 (2.2)	11.9 (2.4)	10.8 (1.0)	7.7 (1.7)	5.1 (-0.1)
Gross Domestic Product	-2.7	7.0	8.0 (1.9)	6.7 (1.9)	6.9 (0.9)	6.4 (1.5)	7.2 (2.8)
<i>Change in the main price indicators (%)</i>							
GDP deflator	-0.6	0.5	0.9 (1.1)	-1.9 (-2.4)	1.7 (2.3)	1.1 (0.2)	1.4 (1.2)
Composite CPI							
Headline	0.5	2.4[@]	1.9 (0.9)	2.6 (0.5)	2.3 (-1.3)	2.7[@] (3.7)[@]	3.8[@] (1.8)[@]
Underlying[^]	1.0	1.7[@]	0.8 (0.6)	1.5 (0.4)	2.0 (0.4)	2.4[@] (1.0)[@]	3.7[@] (1.8)[@]
<u>Change in nominal GDP (%)</u>	-3.3	7.5	8.9	4.7	8.7	7.6	8.8

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.

(@) By reference to the new 2009/10-based CPI series.

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

Table 2

**Economic forecasts for 2011
(rate of change (%))**

	<u>Forecasts for 2011 as released on 23.2.2011</u> (%)	<u>Latest forecasts for 2011 on 13.5.2011</u> (%)
Gross Domestic Product (GDP)		
<i>Real GDP</i>	4 to 5	5 to 6
<i>Nominal GDP</i>	6.5 to 7.5	7.5 to 8.5
Composite Consumer Price Index (CCPI)		
<i>Headline CCPI</i>	4.5	5.4
<i>Underlying CCPI</i>	4.5	5.5
GDP Deflator	2.5	2.5