

Press Release

(embargoed until 4:30 p.m. on 11 November 2011)

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

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

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

MAIN POINTS

- * The Hong Kong economy grew by 4.3% in real terms in the third quarter of 2011 over a year earlier. Though broadly on par with the trend growth over the past ten years, it represented a further moderation from the 5.3% growth in the second quarter. The growth moderation was mainly dragged by a sharp fall-off in exports towards the quarter end amid an increasingly austere global economic environment. The domestic sector nevertheless displayed remarkable resilience throughout the quarter, thereby rendering a strong cushion to overall economic performance. On a seasonally adjusted quarter-to-quarter basis, GDP still expanded slightly by 0.1% in real terms in the third quarter, after a 0.4% decline in the second quarter.
- * Total exports of goods slackened to a modest year-on-year decline of 2.2% in real terms in the third quarter. Not only that exports to the US and EU markets went down further, the second round effects of their sluggish final demand were also increasingly evident across many Asian markets. The ensuing deceleration in regional production resulted in a notable fall-off in Hong Kong's raw material exports to Asia, thereby exacerbating further the weakness in overall export performance.
- * Exports of services were nevertheless resilient, expanding at a solid pace of 6.6% year-on-year in real terms. Exports of travel services maintained double-digit growth on the back of vibrant inbound tourism. Exports of financial and business services continued to see appreciable growth, despite heightened volatilities in the global financial markets during the quarter. Exports of transportation and trade-related services however suffered more from slowing regional trade flows.
- * Domestic demand held up remarkably well and remained the key growth driver in the third quarter. Private consumption expenditure grew robustly further, by 8.8% in real terms over a year earlier, under the support of rising incomes and job growth. Overall investment spending picked up to a double-digit growth at 10.2% in real terms, with strong machinery and equipment acquisition and

infrastructure construction offsetting the slack in private construction activities.

- * The labour market showed broad-based improvements during the quarter. Total employment rose successively to new record highs, pushing the seasonally adjusted unemployment rate down to 3.2% in the third quarter, the lowest in 13 years. With the labour market in a state of full employment, employment earnings showed notable growth across many sectors and occupation categories. Average employment earnings of full-time employees went up markedly by 8.1% in the third quarter over a year earlier. Those in the lowest decile group enjoyed an even higher income growth of 13.1%, reflecting the additional boost from the implementation of the statutory minimum wage.
- * The local stock market underwent a sharp correction during the quarter, as global economic sentiment was severely dented by the deepening eurozone debt crisis and mounting concern over the increasingly shaky global economic recovery. Local property market also turned quieter, with residential flat prices and transaction volume both recording declines.
- * The external environment has deteriorated substantially since the last forecast review in mid-August. The negative impacts on the global economy caused by the eurozone sovereign debt crisis and the ensuing global financial turbulence have intensified towards the end of the third quarter, and are likely to remain pronounced in the period ahead. While the eurozone debt problem will remain a key threat to the global economic outlook, the weakness in the US economy also warrants concern. In Asia, the region as a whole has stayed relatively resilient, but growth has also moderated as a result of weakening external demand. Against the headwinds from such an austere global economic environment, Hong Kong's export outlook in the fourth quarter is bleak.
- * Domestic demand as well as inbound tourism are however expected to hold up better. This, coupled with continued hectic pace in infrastructure investment, should render some cushion against the expected setback in external trade in the fourth quarter. Having regard to the actual outturn of a 5.6% GDP growth in the first three quarters of 2011, and with due cognizance of a still lacklustre export performance in the fourth quarter, the economy is now forecast to grow by 5% for 2011 as a whole, the lower bound of the earlier range forecast of 5-6% in the August round.
- * As part of a region-wide phenomenon, underlying consumer price inflation kept increasing so far this year, reaching 6.1% in the third quarter, and averaging at 4.9% in the first nine months. The pace of rising inflation nevertheless moderated towards the end of the third quarter, thanks to the slight ease-back in food inflation after an almost uninterrupted rise over the past year.
- * The continued ease-back in global food and commodity prices in recent months is a positive development, which in the course of time should help alleviate imported inflation. However, with the lagged effects from the earlier surge in market rentals still feeding through, inflation is likely to edge up slightly further

in the near term before peaking out. Judging from the actual outturn so far and the latest trend in global food prices, the forecast rates of headline and underlying consumer price inflation for 2011 as a whole are marked down slightly to 5.2% and 5.3% respectively, from 5.4% and 5.5% in the August round.

DETAILS

GDP

According to preliminary data on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, real GDP grew by 4.3% in real terms in the third quarter of 2011 over a year earlier, moderated further from the 5.3% growth in the second quarter (revised upwards from the earlier estimate of 5.1%). Taking the first three quarters of 2011 together, real GDP expanded by 5.6% over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, real GDP showed a slight increase of 0.1% in the third quarter, after a mild contraction of 0.4% in the second quarter (revised upwards from the earlier estimate of a 0.5% decline) (*Chart*).

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

External trade

3. *Total exports of goods* slackened further in the third quarter to a 2.2% decline in real terms over a year earlier, from virtually zero growth in the second quarter. Exports to the US saw another quarter of noticeable decline, curtailed by the sluggish demand there. The decline in exports to the EU enlarged further, reflecting the sluggishness and weak sentiment in many EU member economies. Exports to a number of Asian markets, including the Mainland, also slowed, due to the fall-off in intra-regional exports and raw material intake which were closely tied to demand in the developed markets. Exports to Japan however showed some relative improvement, as the post-earthquake recovery proceeded. Exports to Taiwan and India maintained appreciable growth. In general, exports of consumer and capital goods to Asia held up relatively better, though not sufficient to make up for the lull in the developed markets. On a seasonally adjusted quarter-to-quarter comparison, total exports of goods were broadly unchanged in real terms in the third quarter.

4. *Exports of services* were more resilient, maintaining a solid growth of 6.6% in real terms in the third quarter, following a 7.7% growth in the second quarter. Exports of travel services provided the main growth impetus, thanks to vibrant inbound tourism. Exports of financial and business services had further appreciable growth, despite heightened global financial market volatilities during the quarter. Exports of transportation and trade-related services (comprising mainly

offshore trade activities) were however more significantly hit by the slowdown in global trade flows in the quarter. On a seasonally adjusted quarter-to-quarter basis, exports of services grew by 1.1% in real terms in the third quarter.

Domestic sector

5. The domestic sector displayed remarkable strength throughout the third quarter, thereby rendering the key support to overall economic performance. Local consumer sentiment held firm, thanks to the further improvement in job and income conditions. *Private consumption expenditure* grew robustly further by 8.8% in real terms in the third quarter over a year earlier, following the 9.7% growth in the second quarter. On a seasonally adjusted quarter-to-quarter basis, private consumption expenditure grew further by 1.1% in real terms in the third quarter. *Government consumption expenditure* maintained modest growth at 1.7% in real terms over a year earlier.

6. *Overall investment spending* picked up to a strong growth of 10.2% in real terms in the third quarter over a year earlier, further to the 7.0% growth in the second quarter. This was underpinned by a hectic expansion of machinery and equipment investment, by 26.4% year-on-year. Overall building and construction expenditure was virtually unchanged from a year earlier in real terms in the third quarter, after the 5.4% decline in the second quarter. Public sector works continued apace, thereby offsetting the shrinkage in private sector construction activity in the quarter.

The labour sector

7. The labour market showed broad-based and notable improvements, marked by hectic job creation following a period of above-trend economic growth over the past year or so. Total employment rose to successive record highs during the quarter, pushing the *seasonally adjusted unemployment rate* down to 3.2% in the third quarter, the lowest in 13 years. The *underemployment rate* also inched down to 1.7% in the third quarter from 1.8% in the preceding quarter. In tandem with a relatively tight labour market, wages and earnings rose visibly further across all major sectors and occupation categories. Median household income surged by 11.1% year-on-year in the third quarter, the fastest since 1997. Over the same period, average employment earnings of full-time employees went up markedly by 8.1% over a year earlier. Those in the lowest decile group enjoyed an even higher income growth of 13.1%, reflecting the additional boost from the implementation of the statutory minimum wage.

The asset markets

8. The *local stock market* experienced much volatility and underwent a sharp sell-off along with many major overseas markets during the third quarter. Global financial markets were in turmoil under the slackening global economic recovery and the escalating European debt crisis, and the consequential return of risk

aversion and flight to safer assets pushed worldwide stock markets lower. The Hang Seng Index (HSI) shed 21.5% from end-June to close at 17 592 points at end-September, 23.6% lower than the level at end-2010.

9. The *residential property market* showed some consolidation in the third quarter, amid increased headwinds in the external environment and tighter mortgage loan terms offered by local banks. Overall flat prices fell by 2% between June and September 2011, the first quarterly decline since the fourth quarter of 2008. Transactions in the third quarter plunged by 41% over the preceding quarter, reflecting the more cautious market sentiment. Over the same period, flat rentals notched up by a slower rate of 2%, while office and shop rentals rose by 6% and 2% respectively.

Prices

10. Consumer price inflation went up further in the third quarter under the influences of both local and external factors, although the pace of rising inflation showed some initial signs of slowing towards the end of the quarter amid a slight ease-back of food inflation. Domestically, the lagged effects from earlier surge in private housing rentals continued to feed through, while wages also picked up visibly on the back of a tight labour market. On the external front, increase in import prices remained elevated owing to the earlier surge in global food and commodity prices. *Headline consumer price inflation* rose from 5.2% in the second quarter to 6.4% in the third quarter. Netting out the effects of the Government's relief measures, *underlying consumer price inflation* went up from 5.0% to 6.1%.

Latest GDP and price forecasts for 2011

11. The external environment has deteriorated substantially since the last forecast review in mid-August. The negative impacts on the global economy caused by the eurozone sovereign debt crisis and the ensuing global financial turbulence have intensified towards the end of the third quarter, and are likely to remain pronounced in the period ahead. While the eurozone debt problem will remain a key threat to the global economic outlook, the weakness in the US economy also warrants concern. In Asia, the region as a whole has stayed relatively resilient, but growth has also moderated as a result of weakening external demand. Against the headwinds from such an austere global economic environment, Hong Kong's export outlook in the fourth quarter is bleak.

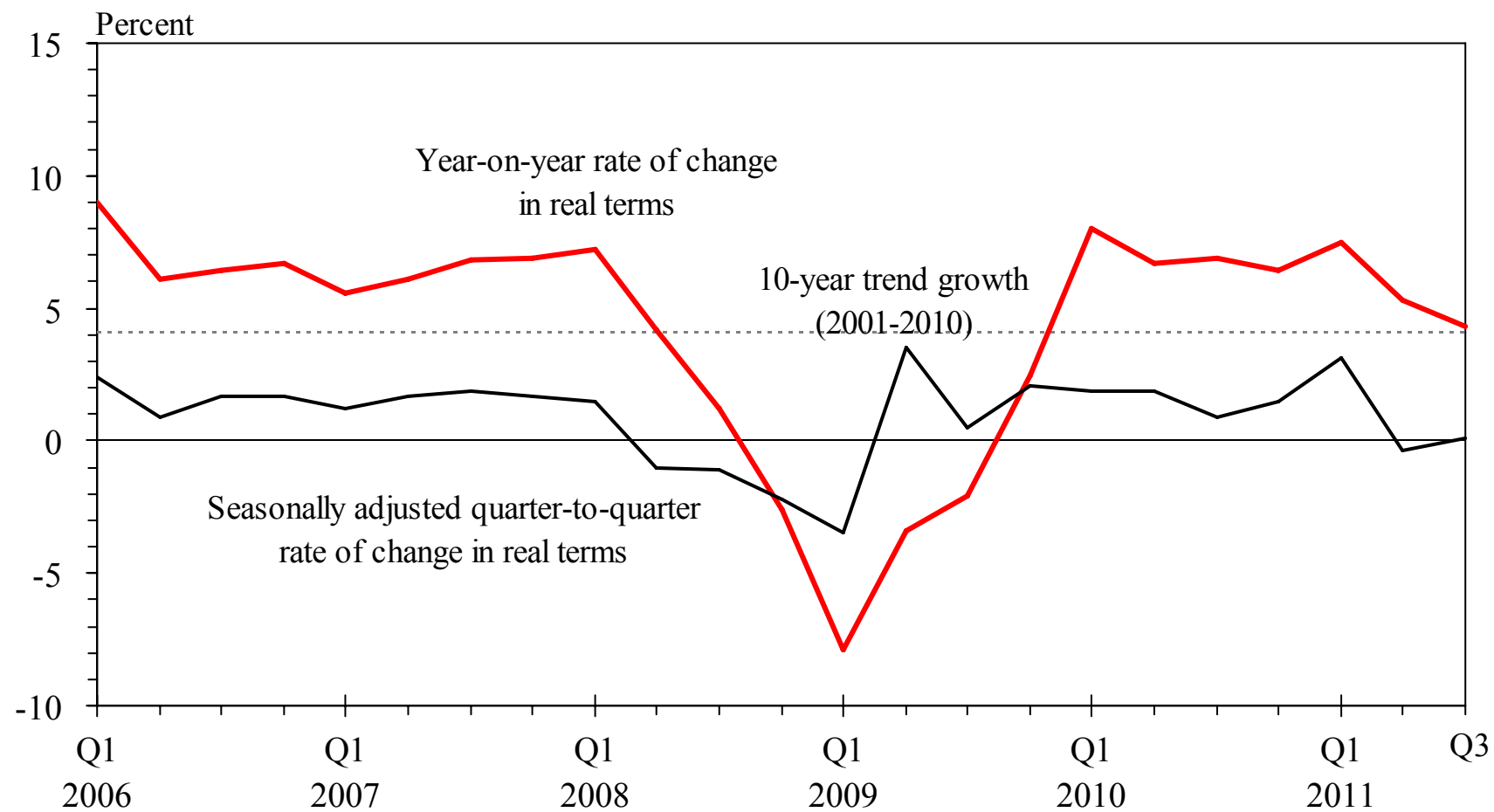
12. Domestic demand as well as inbound tourism are however expected to hold up better. This, coupled with continued hectic pace in infrastructure investment, should render some cushion against the expected setback in external trade in the fourth quarter. Having regard to the actual outturn of a 5.6% GDP growth in the first three quarters of 2011, and with due cognizance of a still lacklustre export performance in the fourth quarter, the economy is now forecast to grow by 5% for 2011 as a whole, the lower bound of the earlier range forecast of

5-6% in the August round (*Table 2*). For reference, the latest forecasts by private sector analysts mostly range from 5-5.5%, averaging at around 5.2%.

13. On inflation outlook, the continued ease-back in global food and commodity prices in recent months is a positive development, which in the course of time should help alleviate imported inflation. However, with the lagged effects from the earlier surge in market rentals still feeding through, inflation is likely to edge up slightly further in the near term before peaking out. Judging from the actual outturn so far and the latest trend in global food prices, the forecast rates of headline and underlying consumer price inflation for 2011 as a whole are marked down slightly to 5.2% and 5.3% respectively, from 5.4% and 5.5% in the August round (*Table 2*).

(The Third 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 \$116 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, Third Quarter 2011, which contains the GDP figures up to the third 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 third 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>	<u>Q2[#]</u>	<u>Q3⁺</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)	8.0 (1.0)	9.7 (2.8)	8.8 (1.1)
Government consumption expenditure	2.3	2.7	3.3 (0.9)	2.7 (0.8)	3.2 (0.9)	1.6 (-0.8)	2.6 (1.8)	1.2 (-0.7)	1.7 (1.3)
Gross domestic fixed capital formation	-3.9	7.8	8.2	15.8	-0.3	8.6	-0.3	7.0	10.2
<i>of which :</i>									
Building and construction	-5.5	6.6	-7.1	13.2	9.6	11.3	16.0	-5.4	*
Machinery, equipment and computer software	-3.0	5.9	11.5	15.9	-7.3	6.4	-12.1	17.5	26.4
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)	0.3 (-11.1)	-2.2 (*)
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)	2.6 (-5.9)	1.4 (-1.0)
Exports of services	0.3	15.0	18.4 (4.1)	17.5 (2.2)	15.8 (2.2)	9.3 (0.3)	9.3 (4.1)	7.7 (0.9)	6.6 (1.1)
Imports of services	-4.9	10.4	11.2 (2.2)	11.9 (2.4)	10.8 (1.0)	7.7 (1.7)	5.8 (0.6)	3.2 (-0.1)	2.1 (-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)	7.5 (3.1)	5.3 (-0.4)	4.3 (0.1)
<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)	1.2 (1.0)	5.0 (1.5)	4.3 (1.4)
Composite CPI									
Headline	0.5	2.4[@]	1.9 (0.8)[@]	2.6 (0.5)[@]	2.3 (-2.2)[@]	2.7[@] (3.7)[@]	3.8[@] (1.8)[@]	5.2[@] (1.8)[@]	6.4[@] (-0.9)[@]
Underlying[^]	1.0	1.7[@]	0.8 (0.5)[@]	1.5 (0.5)[@]	2.0 (0.4)[@]	2.4[@] (1.0)[@]	3.7[@] (1.8)[@]	5.0[@] (1.8)[@]	6.1[@] (1.5)[@]
Change in nominal GDP (%)	-3.3	7.5	8.9	4.7	8.7	7.6	8.7	10.5	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.

(*) Change of less than 0.05%.

(@) 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 (%))**

	Forecasts for 2011 as released on <u>12.8.2011</u> (%)	Latest forecasts for 2011 on <u>11.11.2011</u> (%)
Gross Domestic Product (GDP)		
<i>Real GDP</i>	5 to 6	5
<i>Nominal GDP</i>	7.5 to 8.5	7.5
Composite Consumer Price Index (CCPI)		
<i>Headline CCPI</i>	5.4	5.2
<i>Underlying CCPI</i>	5.5	5.3
GDP Deflator	2.5	2.5