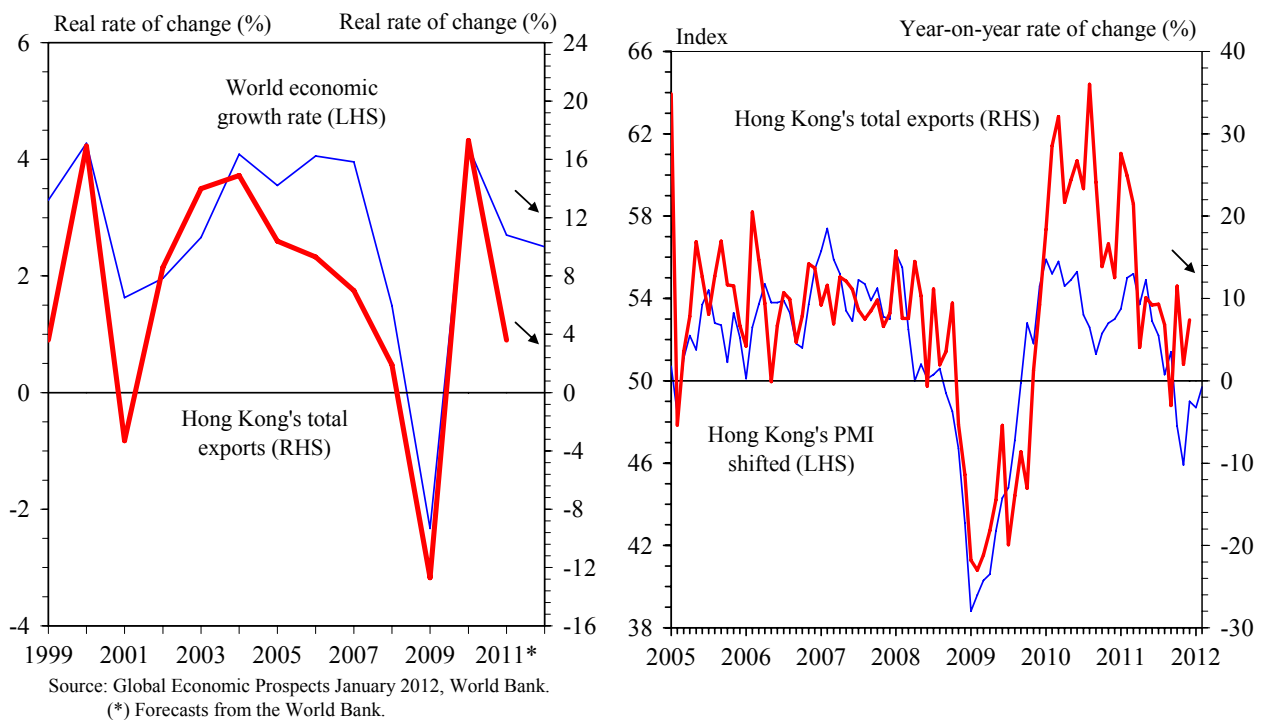


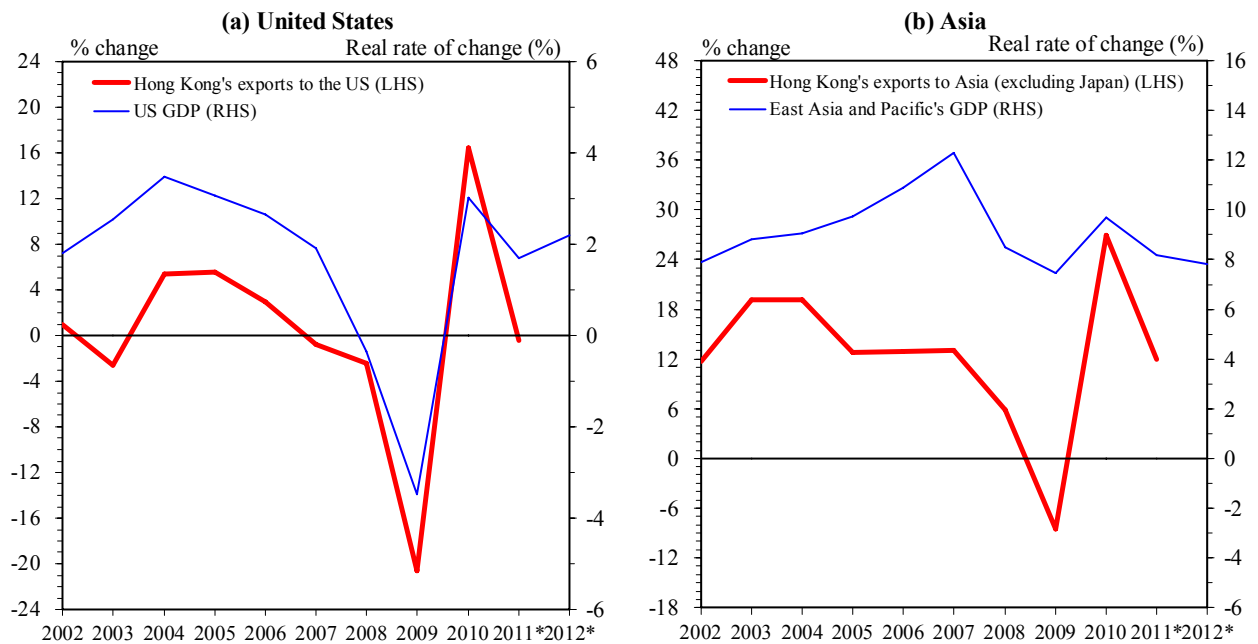
## Outlook for the Hong Kong economy in 2012

2.22 Given the highly externally-oriented nature of the Hong Kong economy, its performance is closely tied to the demand conditions of its major economic partners. The external environment has deteriorated visibly over the course of 2011, with the eurozone sovereign debt crisis emerging as an imminent source of threat to the global economy and with the recovery in the US remaining unsteady. In face of increasing headwinds on the external front, the outlook for Hong Kong's *exports of goods* in 2012 is bleak. To what extent merchandise trade will be undermined hinges crucially on how the euro debt crisis will evolve and spill over to other economies, notably the US, for which Europe is a major trading partner. In any case, even if the debt crisis can be contained without unravelling in a disorderly fashion, the austerity measures required in the debt-stricken countries will pose a heavy drag on demand from Europe to the detriment of Asian exports, including Hong Kong's. Yet many Asian economies have relatively more room for policy manoeuvre, and granting that a full-blown euro debt crisis does not materialise, the Asian markets should provide some cushion to Hong Kong's external sector especially in the latter part of 2012.

**Diagram 2.6 : The outlook for Hong Kong's exports of goods in 2012 is bleak**



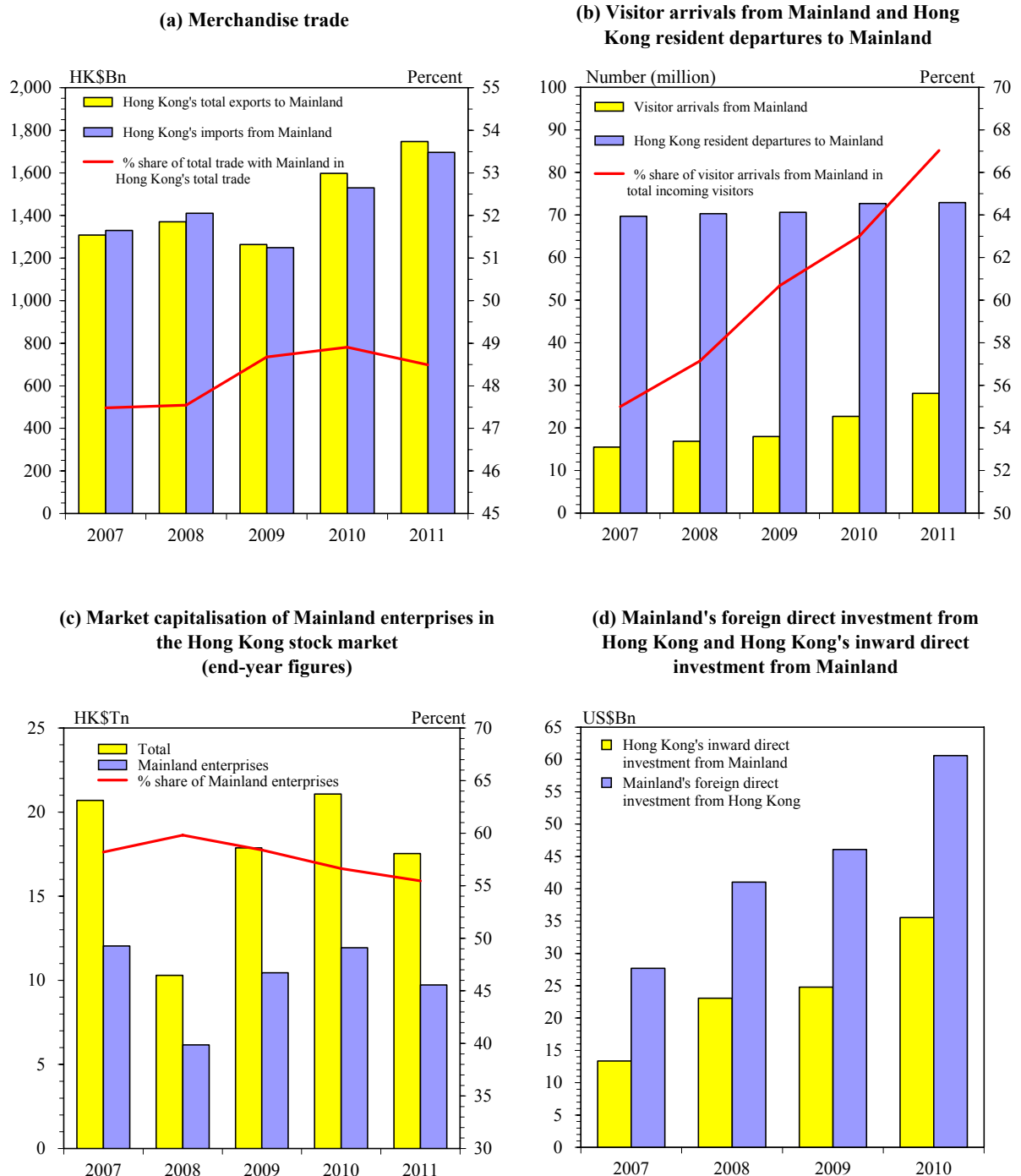
**Diagram 2.7 : Exports to the Asian markets should provide some cushion to the expected weakness in the advanced markets**



Note: (\*) Forecasts from the Global Economic Prospects January 2012, World Bank.

2.23 The performance of *exports of services* has been more resilient, underscoring the strong competitiveness of Hong Kong's services sector on the back of deepening integration with the Mainland. As such, exports of services should be less vulnerable to weaker external demand in 2012. In particular, inbound tourism is expected to stay vibrant, in view of the prevailing strong influx of visitors from the Mainland. Exports of financial and business services, despite the envisaged continuation of financial market volatilities, should still be able to benefit from the further development of renminbi business in Hong Kong and cross-border commercial activity. However, offshore trade and exports of transportation services will likely show weaker performance in tandem with the expected slowdown in global and regional trade flows.

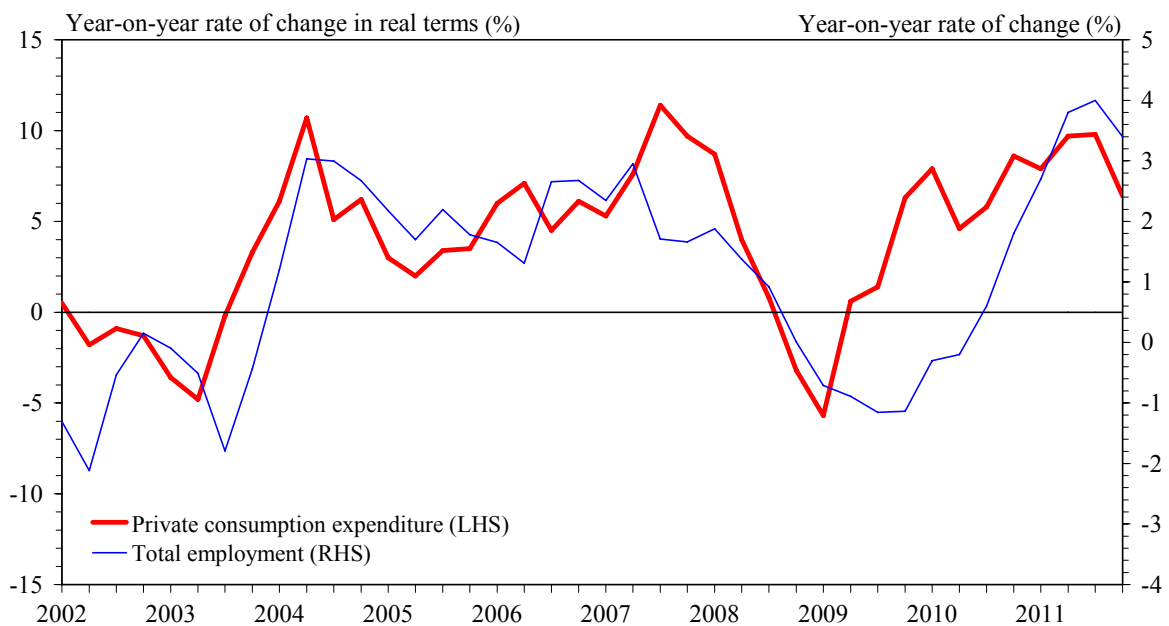
**Diagram 2.8 : The Mainland factor will continue to be a key supportive factor for the Hong Kong economy**



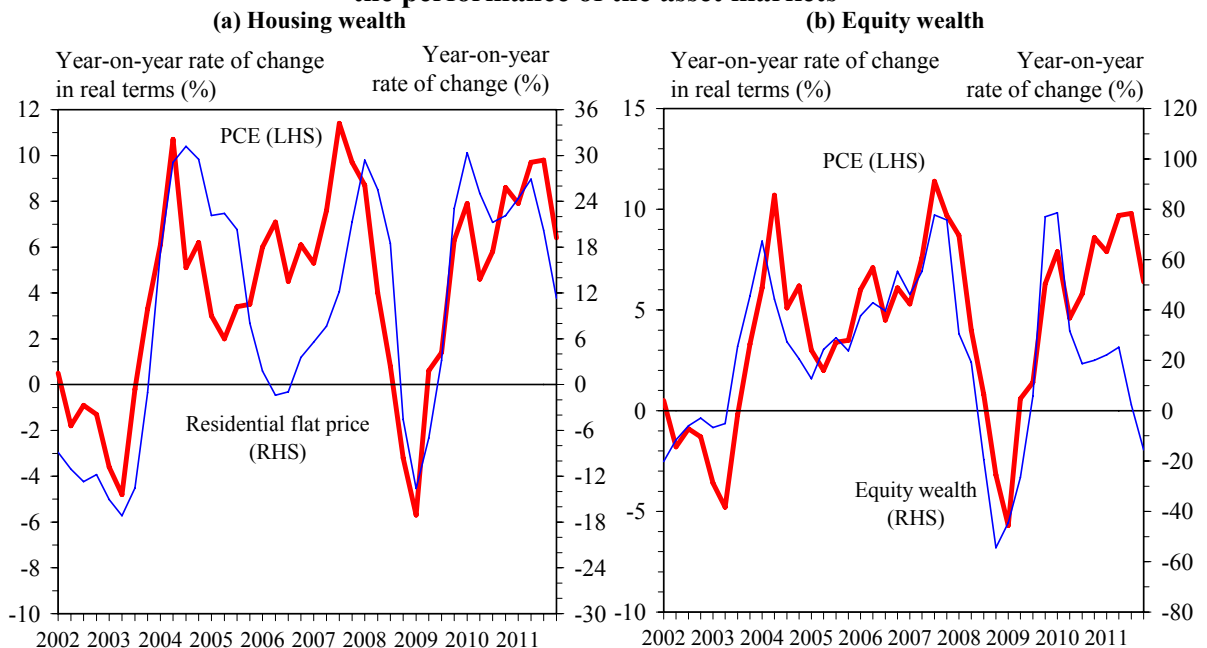
2.24 *Domestic demand* held up remarkably well throughout 2011 and served as a key growth driver. In the light of the notable employment and income growth over the past year or so, local consumption spending will likely hold up relatively better and provide some buffer to the expected weakness in the external sector. That said, the level of resilience displayed by consumption spending will also hinge on the local labour market situation down the road now that employers' hiring sentiment has turned more cautious of late, and also on the performance of the local asset markets amid the strong headwinds in the

external environment. As for investment, machinery and equipment acquisition, being more susceptible to the business cycle, is expected to slacken in the near term. Indeed, the results of the latest Quarterly Business Tendency Survey conducted by the Census and Statistics Department indicated that many of the large companies surveyed have turned more pessimistic about their near-term business outlook. Nevertheless, the building and construction component should continue to be underpinned by the intensive public sector infrastructure works, thereby rendering an additional cushion to the domestic economy.

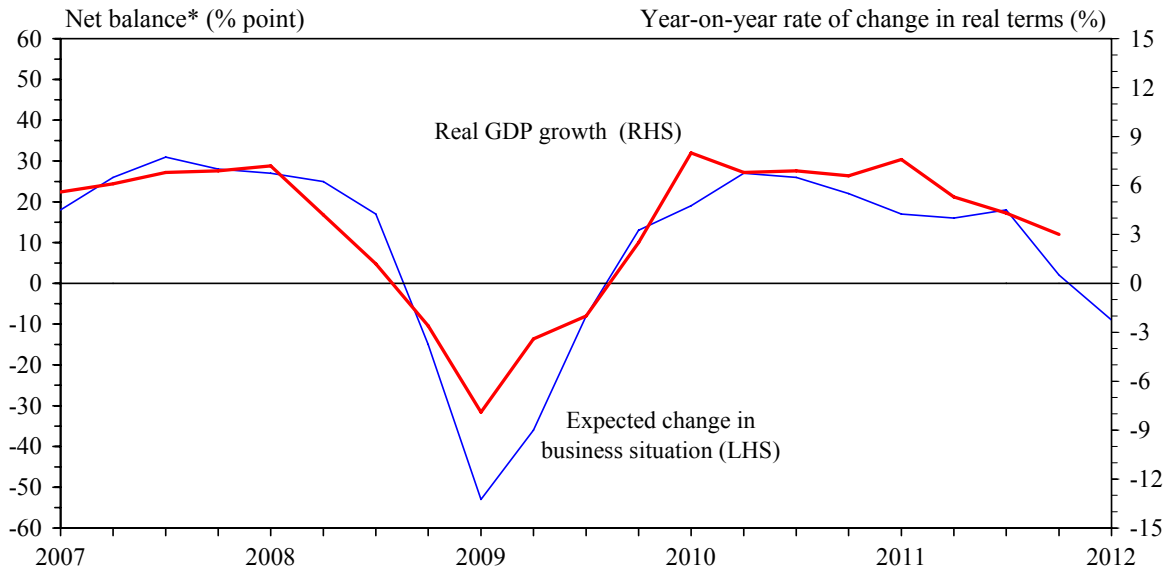
**Diagram 2.9 : Private consumption should hold up relatively better, thanks to the notable employment growth over the past year or so**



**Diagram 2.10 : Yet consumer sentiments will also hinge on the performance of the asset markets**

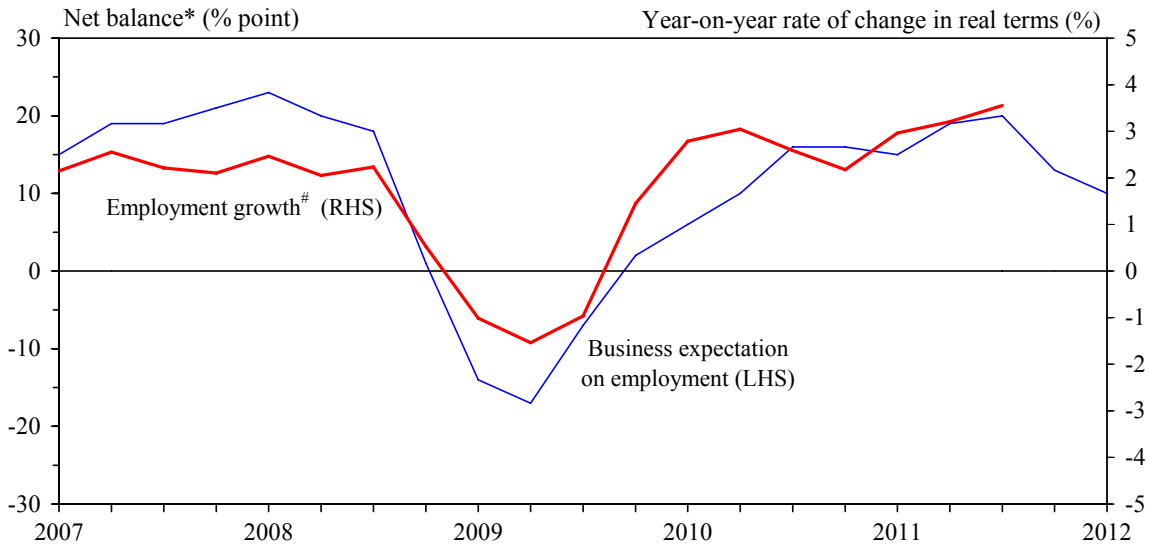


**Diagram 2.11 : Business sentiment has turned more pessimistic of late**



Note : (\*) Net balance indicates the direction of expected change in business situation versus preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "better" over that choosing "worse". A positive sign indicates a likely upward trend while a negative sign, a likely downward trend.

**Diagram 2.12 : Businesses are also more cautious towards hiring**

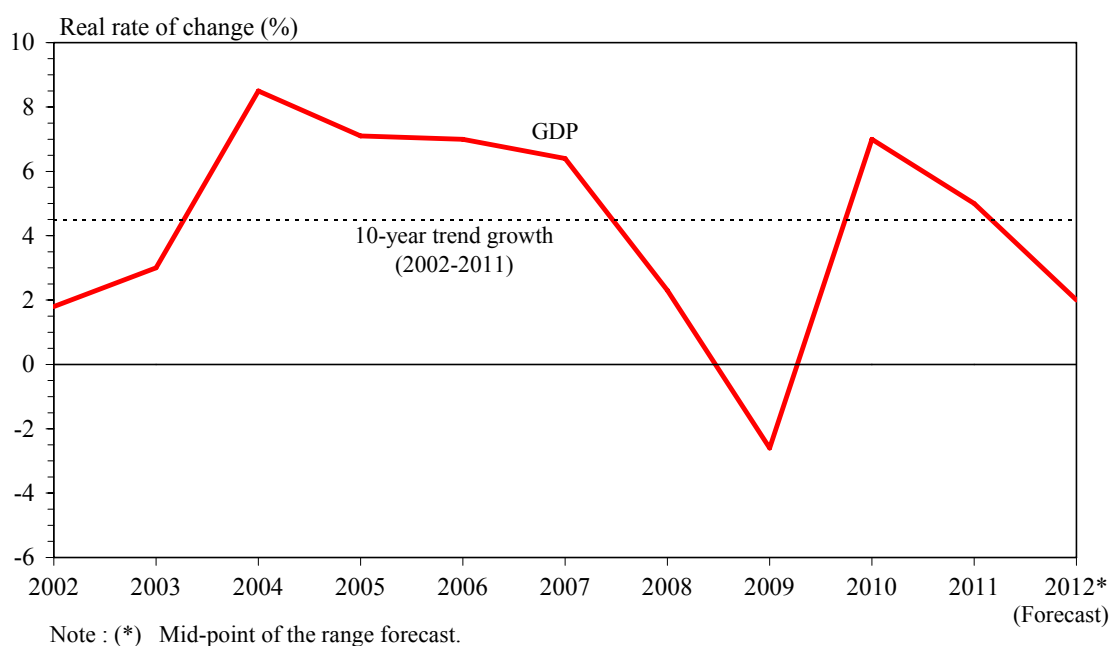


Notes : (\*) Net balance indicates the direction of expected change in number of persons engaged versus preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "up" over that choosing "down". A positive sign indicates a likely upward trend while a negative sign, a likely downward trend.  
 (#) Employment in private sector.

2.25 Taking all these developments together, and barring the adverse development of the euro debt problem into a full-blown crisis, the Hong Kong economy is projected to show a more muted growth of 1-3% in 2012. This will be lower than the average growth of 4.5% in the past ten years and the prevailing forecasts by private sector analysts, which mostly fall within the range of 1.5% to 3.5%. The wider than usual range of growth forecast signifies

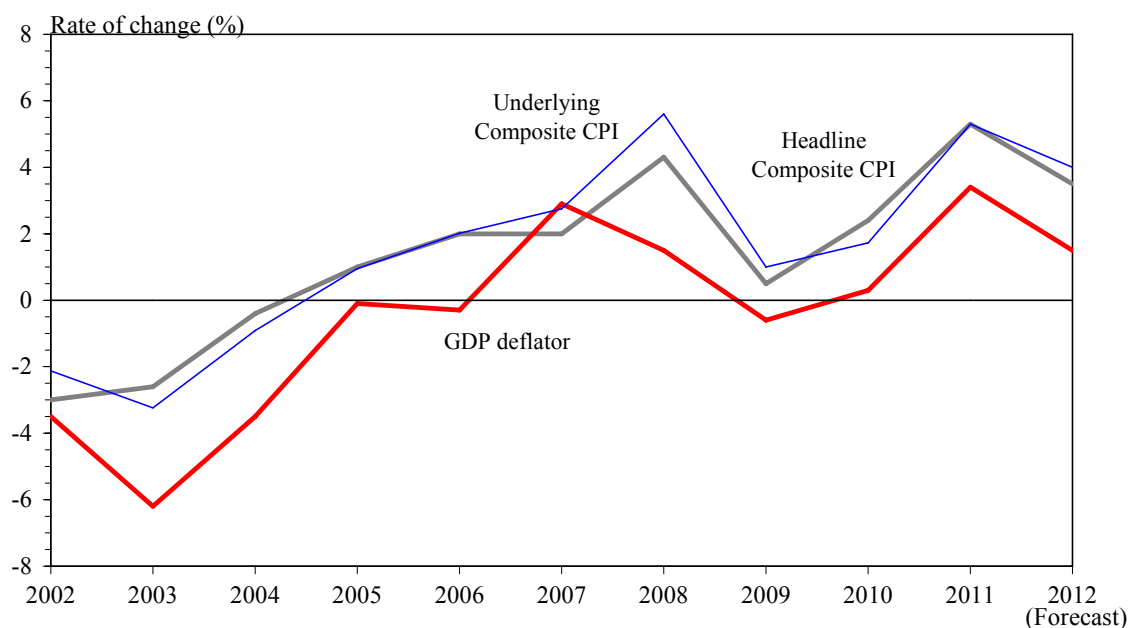
the unusually high degree of uncertainty facing the economy, mainly stemming from the fluidity of the eurozone debt situation and the ongoing fiscal consolidation in the advanced economies, as detailed in paragraph 2.21. The balance of forces will hinge on how well domestic demand and services exports, as well as the Asian markets, can hold up and to what extent they will offset the severe drag from goods exports due to the dire situations in the advanced economies.

**Diagram 2.13 : Economy expected to show only muted growth in 2012**



2.26 Inflation in Hong Kong has largely stabilised towards the end of 2011. Judging from the current trend, underlying inflation should come down over the course of 2012. On the external front, upward pressures on global commodity prices have largely abated given the subdued growth outlook in 2012. Global food prices, in particular, have broadly stabilised recently. Domestically, private housing rentals, after surging notably during 2010 and in the first half of 2011, have shown signs of tapering off of late alongside the consolidation in the local property market, although this favourable development would take time to show up in consumer price inflation. Furthermore, with the local economy poising for sub-par growth, wage cost pressures should also turn less notable. Overall, the *underlying Composite CPI* is forecast to increase by 4.0% for 2012 as a whole. Taking into account the effects of the Government's relevant one-off measures, the *headline Composite CPI* is forecast to increase by 3.5%. The *GDP deflator* is forecast to rise by 1.5%, largely on account of the slower increase of domestic prices as well as the expected change in the terms of trade.

**Diagram 2.14 : Inflation is expected to ease off in 2012, with both external and domestic price pressures subsiding**



**Forecast rate of change in 2012 (%)**

**Gross Domestic Product (GDP)**

<i>Real GDP</i>	<b>1 to 3</b>
<i>Nominal GDP</i>	<b>2.5 to 4.5</b>
<i>Per capita GDP, in real terms</i>	<b>0.1 to 2.1</b>
<i>Per capita GDP at current market prices</i>	<b>HK\$270,400-275,700 (US\$34,700-35,300)</b>

**Composite Consumer Price Index**

<i>Headline</i>	<b>3.5</b>
<i>Underlying</i>	<b>4.0</b>

**GDP Deflator**

**1.5**

**Forecast on Hong Kong's GDP growth in 2012 recently made by other selected parties**

	(%)
The University of Hong Kong	2 to 3
Average forecast by private sector analysts <sup>#</sup>	3.3

Note: (#) Forecast GDP growth by private sector analysts mostly falls between 1.5% and 3.5%.

## ECONOMIC PERFORMANCE IN 2011

1. Estimated rates of change in the Gross Domestic Product and its expenditure components and in the main price indicators in 2011:

	(%)
(a) Growth rates in real terms of:	
Private consumption expenditure	8.4
Government consumption expenditure	1.8
Gross domestic fixed capital formation	7.3
Total exports of goods	3.6
Imports of goods	4.8
Exports of services	6.3
Imports of services	3.0
<b>Gross Domestic Product (GDP)</b>	<b>5.0</b>
<i>Per capita GDP in real terms</i>	4.4
<i>Per capita GDP at current market prices</i>	HK\$266,000 (US\$34,200)
(b) Rates of change in:	
<b>Composite Consumer Price Index</b>	<b>5.3</b>
<b>GDP Deflator</b>	<b>3.4</b>
<b>Government Consumption Expenditure Deflator</b>	<b>4.9</b>
(c) <b>Growth rate of nominal GDP</b>	<b>8.6</b>



2. Annual growth rates in real terms of re-exports and domestic exports based on external trade quantum index numbers <sup>(Note 1)</sup>:

	<b>Re-exports</b> (%)	<b>Domestic exports</b> (%)
2009	-11	-35
2010	18	16
2011	4	-22
<i>Share in the value of total exports of goods in 2011</i>	98	2

3. Annual growth rates in real terms of retained imports by type <sup>(Note 1)</sup>:

	<b>Retained imports</b>					
	<b>Total</b> (%)	<b>Consumer goods</b> (%)	<b>Foodstuffs</b> (%)	<b>Capital goods</b> (%)	<b>Raw materials and semi-manufactures</b> (%)	<b>Fuels</b> (%)
2009	-4	-9	7	-4	-10	23
2010	20	22	12	16	31	14
2011	9	24	2	15	-9	-11

4. Annual growth rates in real terms of retained imports of capital goods by type <sup>(Note 1)</sup>:

	<b>Retained imports of capital goods</b>				
	<b>Total</b> (%)	<b>Office equipment</b> (%)	<b>Industrial machinery</b> (%)	<b>Construction machinery</b> (%)	<b>Telecommunications equipment</b> (%)
2009	-4	-9	-31	63	5
2010	16	-6	12	18	27
2011	15	-15	-11	-10	25

Note 1 Figures for 2011 are estimates based on actual unit value indices up to November 2011. They are subject to revision when the full-year data become available.

5. Annual growth rates in real terms of exports of services by type <sup>(Notes 2 & 3)</sup>:

*Exports of services*

	<i>Total</i> (%)	<i>Trade-related</i> <i>services</i> (%)	<i>Transportation</i> <i>services</i> (%)	<i>Travel</i> <i>services</i> (%)	<i>Finance,</i> <i>insurance,</i> <i>business and</i> <i>other services</i> (%)
2009	0	-5	-2	8	5
2010	15	13	8	26	16
2011	6	—	—	—	—

6. Hong Kong's visible and invisible trade balance in 2011 reckoned on GDP basis <sup>(Note 2)</sup>:

	(HK\$ billion)
Total exports of goods	3,409.2
Imports of goods	3,846.5
<b><i>Visible trade balance</i></b>	<b>-437.3</b>
Exports of services	940.5
Imports of services	434.5
<b><i>Invisible trade balance</i></b>	<b>506.0</b>
<b><i>Combined visible and invisible trade balance</i></b>	<b>68.8</b>

Note 2 Advance preliminary figures.

Note 3 As the compilation of the figures of exports of services for 2011 as a whole has been advanced, breakdown figures of major service groups are not available.

7. Annual averages of the unemployment and underemployment rates and growth in labour force and total employment:

	<i>Unemployment rate (%)</i>	<i>Underemployment rate (%)</i>	<i>Growth in labour force (%)</i>	<i>Growth in total employment (%)</i>
2009	5.4	2.3	0.8	-1.1
2010	4.4	2.0	-0.6	0.4
2011	3.4	1.7	2.6	3.7

8. Annual rates of change in the Consumer Price Indices:

	<i>Composite CPI</i>		<i>CPI(A)</i>	<i>CPI(B)</i>	<i>CPI(C)</i>
	<i>Headline (%)</i>	<i>Underlying (%)</i>	<i>(%)</i>	<i>(%)</i>	<i>(%)</i>
2009	0.5	1.0	0.4	0.5	0.6
2010	2.4	1.7	2.7	2.3	2.1
2011	5.3	5.3	5.6	5.2	5.1

## ECONOMIC PROSPECTS FOR 2012

Forecast rates of change in the Gross Domestic Product and prices in 2012:

	(%)
<b>Gross Domestic Product (GDP)</b>	
<i>Real GDP</i>	<b>1 to 3</b>
<i>Nominal GDP</i>	2.5 to 4.5
<i>Per capita GDP in real terms</i>	0.1 to 2.1
<i>Per capita GDP at current market prices</i>	HK\$270,400-275,700 (US\$34,700-35,300)
<b>Composite Consumer Price Index</b>	
<i>Headline Composite Consumer Price Index</i>	<b>3.5</b>
<i>Underlying Composite Consumer Price Index</i>	<b>4.0</b>
<b>GDP Deflator</b>	<b>1.5</b>
<b>Government Consumption Expenditure Deflator</b>	<b>4.0</b>