

## Press Release

(embargoed until 4:30 p.m. on 15 August 2014)

### **Economic Situation in the Second Quarter of 2014 and Latest GDP and Price Forecasts for 2014**

The Government released today (Friday) the Half-yearly Economic Report 2014, together with the preliminary figures on Gross Domestic Product for the second quarter of 2014.

The Government Economist, Mrs Helen Chan, described the economic situation in the second quarter of 2014 and provided the latest GDP and price forecasts for the year.

#### **MAIN POINTS**

- \* The Hong Kong economy slowed down further to a mere 1.8% year-on-year growth in real terms in the second quarter of 2014, from 2.6% in the first quarter, marking the slowest growth since the third quarter of 2012. The weak performance was mainly weighed down by a fall-off in tourist spending and a concurrent slowdown in domestic demand. On a seasonally adjusted quarter-to-quarter comparison, real GDP dipped by 0.1% in the second quarter, after a 0.3% growth in the preceding quarter.
- \* Total exports of goods staged a modest pick-up in the second quarter, rising by 2.3% year-on-year in real terms, up from 0.5% in the preceding quarter, though the improvement over the period was brought about mainly by a notable rebound in June. Against this, however, exports of services slackened visibly to a 2.3% year-on-year decline in real terms, upon a double-digit plunge in exports of travel services, though other items showed some relative improvement. This marked the first decline since the second quarter of 2009.
- \* Domestic demand also saw some growth slowdown. Private consumption grew only slightly by 1.2% year-on-year in the second quarter, after two quarters of subdued economic growth. Investment expenditure relapsed to a 5.6% decline, upon a distinct fall in machinery and equipment acquisition, the latter partly affected by an exceptionally high base of comparison a year ago.
- \* The labour market held generally stable. The seasonally adjusted unemployment rate edged up to 3.2% in the second quarter, from 3.1% in the first quarter. Wages and earnings rose further, while average employment earnings for grassroots workers sustained real improvement. While overall employment and income conditions remained favourable in the second quarter, the slowdown in the tourism sector of late and its potential impact on the labour market going forward need to be closely monitored.
- \* The local stock market rallied in recent period, as sentiment improved upon a reviving Mainland economy and the Federal Reserve's reiteration of its accommodative monetary stance. The residential property market firmed up

again, with trading activity rebounding in the second quarter from the lows and prices bouncing back successively.

- \* Looking forward, the global economy is expected to remain on a moderate recovery path in the rest of 2014. This, together with an improving Mainland economy, should entail a somewhat brighter export outlook for Hong Kong in the period ahead, though the scope of rebound might continue to be held back by the rather fragile recovery of the advanced markets.
- \* On the local front, domestic demand is likely to maintain only a rather slow pace of expansion in the second half of the year. Local consumer sentiment may turn somewhat cautious following the economic growth slowdown in recent quarters. As for investment, the results of the latest Quarterly Business Tendency Survey showed that business sentiment weakened in the local consumption-related sectors, while cautiousness lingered in the trade-related sectors, reflecting the headwinds from the still uncertain external environment and the recent abrupt turn in tourism-related sectors.
- \* In cognizance of the worse-than-expected outturn in the first half of 2014, and even taking into account some possible relative stabilisation in economic performance in the latter part of the year, the Hong Kong economy is only poised to attain modest growth for this year as a whole. The GDP growth forecast for 2014 as a whole is thus revised downward from 3-4% in the May round of review to 2-3% in the current round.
- \* At the present juncture, both the local and external environments are beset with increasing downside risks. Externally, the pace of US monetary normalisation remains contingent on incoming economic data, which could shift market expectations about capital flows and interest rates. The recovery of the eurozone economy is still constrained by various structural issues, while in Japan, the economy contracted after the sales tax hike in April, and its development in the period ahead needs to be watched over. Also, geopolitical tensions in various parts of the world have intensified further of late, which would not only curtail economic sentiment, but might also result in abrupt reversals of cross-border fund flows to the detriment of global financial market stability. Locally, while retail business should hopefully turn more stable as the high base effects from last year progressively fade, the distinct slackening in tourist spending of late and the slowdown in domestic demand have emerged as new sources of uncertainty affecting the overall economic outlook.
- \* Underlying consumer price inflation eased further, to 3.5% in the second quarter of 2014 from 3.8% in the preceding quarter. With the modest rise in import prices and weaker economic growth momentum, upside risks to inflation have receded somewhat. Taking into account the actual outturn in the first half of the year, the forecast rates of headline and underlying consumer price inflation for 2014, at 4.6% and 3.7% respectively in the May round, are revised downward in the current round of review, to 4.4% and 3.5% respectively.

## DETAILS

### GDP

According to preliminary data on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, GDP grew by 1.8% in real terms in the second quarter of 2014 over a year earlier, slower than the 2.6% growth in the preceding quarter (revised from the earlier estimate of 2.5%). On a seasonally adjusted quarter-to-quarter comparison, real GDP dipped by 0.1% in the second quarter, after the 0.3% growth in the preceding quarter (revised from the earlier estimate of 0.2%) (*Chart*).

2. The latest figures on GDP and its major expenditure components up to the second quarter of 2014 are presented in *Table 1*. Developments in different segments of the economy in the second quarter of 2014 are described below.

### External trade

3. *Total exports of goods* rose by 2.3% year-on-year in real terms in the second quarter, up from 0.5% in the preceding quarter. The improvement over the period was however brought about mainly by the visible pick-up in June, and also partially offset by the moderation in non-monetary gold exports during the quarter. Exports to the EU and the US expanded further in the second quarter, though only at a modest to moderate pace, reflecting the slow recovery of the advanced economies. While exports to the Mainland resumed growth in May and June, those to most other Asian markets also turned somewhat better, mirroring the relative improvement in the global economic environment during the quarter. On a seasonally adjusted basis, total exports of goods rose by 0.7% in real terms in the second quarter over the preceding quarter.

4. *Exports of services*, on the other hand, slackened abruptly, registering a 2.3% year-on-year decline in real terms in the second quarter, the first decrease since the second quarter of 2009. The setback in exports of travel services was the main drag, with the year-on-year decline magnified further by a distinctly high base of comparison a year ago caused by the spike in visitors' purchases of gold-related items. Indeed, the implied fall in per capita visitor spending was rather noticeable, given the near double-digit rise in the number of visitor arrivals in the quarter. As to other services exports, exports of trade-related services and transportation services improved somewhat, in tandem with the modest recovery of trade flows. Exports of financial and other business services also made modest growth alongside further expansion in cross-border financial activities. On a seasonally adjusted basis, exports of services also fell visibly, by 2.3% in real terms in the second quarter over the preceding quarter.

## **Domestic sector**

5. Domestic demand saw some growth slowdown. *Private consumption expenditure* weakened, following two quarters of economic slowdown, to a 1.2% year-on-year growth in real terms in the second quarter of 2014. On a seasonally adjusted quarter-to-quarter comparison, private consumption expenditure declined by 0.9% in the second quarter. *Government consumption expenditure* maintained steady growth at 2.7% year-on-year in the second quarter.

6. Overall investment spending in terms of *gross domestic fixed capital formation* relapsed to a 5.6% year-on-year decline in real terms in the second quarter, in contrast to the 3.5% growth in the preceding quarter. Within this, the growth in overall building and construction expenditure slowed, as the incremental growth in large-scale infrastructure works tapered after the exceptionally strong growth in preceding quarters, and as private sector building activity grew at a modest pace. At the same time, machinery and equipment acquisition, which was typically volatile, fell notably by 10.0% against an exceptionally high base of comparison in the same period last year, posing a drag on the overall investment spending performance.

## **The labour sector**

7. The labour market held generally stable in the second quarter of 2014. The *seasonally adjusted unemployment rate* edged up to 3.2% in the second quarter, from the 16-year low of 3.1% in the preceding quarter. Meanwhile, the *underemployment rate* rose to 1.5% in the second quarter from a low of 1.3% in the first quarter. Wages and earnings saw further increases in the first quarter. Average employment earnings of grassroot workers sustained real improvement in the second quarter, with those of full-time employees at the unskilled level rising by 2.1% in real terms after discounting inflation. While overall employment and income conditions remained favourable in the second quarter, the slowdown in the tourism sector of late and its potential impact on the labour market going forward need to be closely monitored.

## **The asset markets**

8. The *local stock market* rallied in the more recent period, as the Mainland economy maintained growth momentum and as the Federal Reserve reiterated its stance to maintain accommodative policy for a considerable time after ending its asset purchase programme. Growing optimism about the positive impacts of the forthcoming implementation of Shanghai-Hong Kong Connect scheme further lifted the stock market in July. The Hang Seng Index climbed up successively to 24 757 at end-July, 6% higher than the level at end-2013.

9. The *residential property market* showed some revival in the second quarter. Sentiment improved as market concerns over an imminent US interest rate hike lessened. This, coupled with the launch of several large primary projects by developers at a discount to comparable developments in the secondary market, has helped unleash the pent-up demand. Residential property prices rose by 3% during the second quarter, with overall flat prices in June exceeding the 1997 peak by 44%. Separately, flat rentals increased by 1% during the second quarter, while office rentals stayed flat and shop rentals went up by 3%.

## **Prices**

10. Consumer price inflation continued its easing trend in the second quarter of 2014. Locally, the residential rental pressures subsided further and continued to manifest itself through narrower increases in the private rental component of the consumer price indices. Other domestic costs also saw moderated gains, with year-on-year rises in commercial rentals decelerating further and labour costs keeping a moderate growth pace, helping alleviate pressures on business costs. On the external front, the rise in overall import prices stayed modest, thanks to the generally stable international food and commodity prices and tame inflation in major import sources, notwithstanding some temporary upward movements in global oil prices spurred by heightened geopolitical tensions in the Middle East and Eastern Europe during the quarter. *Headline consumer price inflation* slowed to 3.6% in the second quarter of 2014 from 4.2% in the preceding quarter. For the first half of 2014 as a whole, headline inflation averaged 3.9%, down from 4.3% in 2013. Netting out the effects of the Government's relief measures to more accurately reflect the underlying inflation trend, *underlying consumer price inflation* also eased to 3.5% in the second quarter, from 3.8% in the first quarter. For the first half as a whole, underlying inflation averaged 3.7%, 0.3 percentage point down from that of 4.0% in 2013.

## **Latest GDP and price forecasts for 2014**

11. Looking forward, the global economy is expected to remain on a moderate recovery path in the rest of 2014. This, together with an improving Mainland economy, should entail a somewhat brighter export outlook for Hong Kong in the period ahead, though the scope of rebound might continue to be held back by the rather fragile recovery of the advanced markets.

12. On the local front, domestic demand is likely to maintain only a rather slow pace of expansion in the second half of the year. Local consumer sentiment may turn somewhat cautious following the economic growth slowdown in recent quarters. As for investment, the results of the latest Quarterly Business Tendency Survey showed that business sentiment weakened in the local consumption-related sectors, while cautiousness lingered in the trade-related sectors, reflecting the headwinds from the still uncertain external environment and the recent abrupt turn in tourism-related sectors.

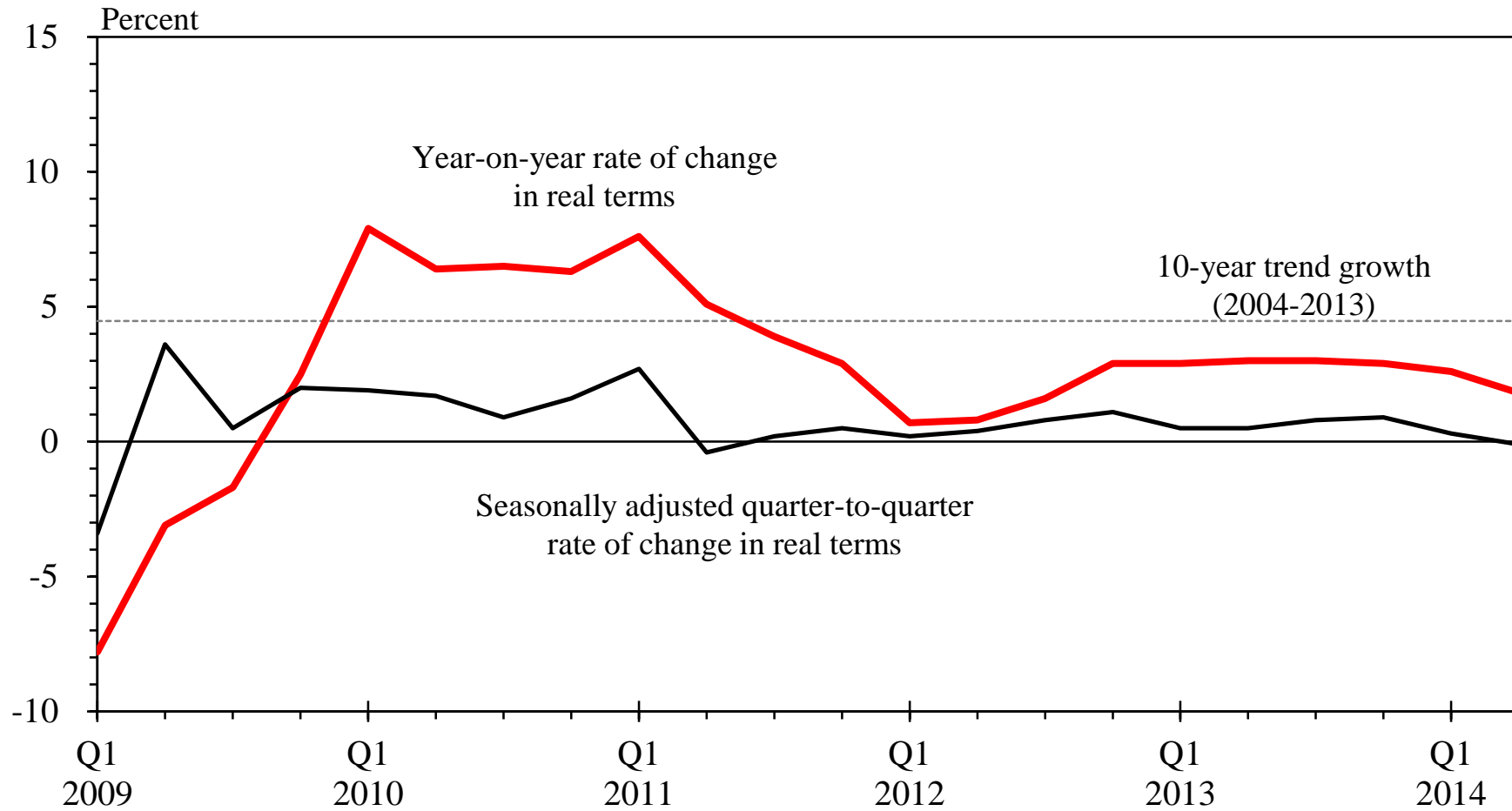
13. In cognizance of the worse-than-expected outturn in the first half of 2014, and even taking into account some possible relative stabilisation in economic performance in the latter part of the year, the Hong Kong economy is only poised to attain modest growth for this year as a whole. The GDP growth forecast for 2014 as a whole is thus revised downward from 3-4% in the May round of review to 2-3% in the current round (*Table 2*). For reference, the latest forecasts by private sector analysts mostly range from 2.5-3.6%, averaging around 3.1%.

14. At the present juncture, both the local and external environments are beset with increasing downside risks. Externally, the pace of US monetary normalisation remains contingent on incoming economic data, which could shift market expectations about capital flows and interest rates. The recovery of the eurozone economy is still constrained by various structural issues, while in Japan, the economy contracted after the sales tax hike in April, and its development in the period ahead needs to be watched over. Also, geopolitical tensions in various parts of the world have intensified further of late, which would not only curtail economic sentiment, but might also result in abrupt reversals of cross-border fund flows to the detriment of global financial market stability. Locally, while retail business should hopefully turn more stable as the high base effects from last year progressively fade, the distinct slackening in tourist spending of late and the slowdown in domestic demand have emerged as new sources of uncertainty affecting the overall economic outlook.

15. On inflation outlook, upside risks to inflation have receded somewhat in the light of the modest rise in import prices and weaker economic growth momentum. Taking into account the actual outturn in the first half of the year, the forecast rates of headline and underlying consumer price inflation for 2014, at 4.6% and 3.7% respectively in the May round, are revised downward in the current round of review, to 4.4% and 3.5% respectively (*Table 2*).

(The Half-yearly Economic Report 2014 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 \$222 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, Second Quarter 2014, which contains the GDP figures up to the second quarter of 2014, 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 second quarter of 2014 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>2012<sup>#</sup></u>	<u>2013<sup>#</sup></u>	<u>2013</u>				<u>2014</u>	
			<u>Q1<sup>#</sup></u>	<u>Q2<sup>#</sup></u>	<u>Q3<sup>#</sup></u>	<u>Q4<sup>#</sup></u>	<u>Q1<sup>#</sup></u>	<u>Q2<sup>+</sup></u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>								
Private consumption expenditure	4.1	4.3	6.3 (2.9)	4.7 (-0.9)	2.7 (-0.2)	3.6 (1.8)	1.5 (0.6)	1.2 (-0.9)
Government consumption expenditure	3.6	2.3	1.9 (*)	3.1 (1.8)	2.3 (*)	2.0 (0.3)	2.6 (0.5)	2.7 (1.9)
Gross domestic fixed capital formation	6.8	3.3	-3.0	7.6	2.7	5.3	3.5	-5.6
<i>of which :</i>								
Building and construction	7.2	-0.9	-1.5	-0.7	3.1	-3.8	10.6	1.3
Machinery, equipment and intellectual property products	10.1	10.8	-4.4	19.8	7.6	17.5	1.9	-10.0
Total exports of goods	1.8	6.6	8.8 (1.5)	6.1 (-1.4)	6.1 (3.2)	5.7 (2.1)	0.5 (-3.4)	2.3 (0.7)
Imports of goods	3.0	7.4	9.5 (3.4)	7.6 (-1.7)	6.6 (1.7)	6.1 (2.3)	1.2 (-0.6)	1.1 (-2.2)
Exports of services	2.2	5.5	4.7 (1.8)	7.7 (3.3)	5.0 (-2.9)	4.7 (2.6)	3.3 (0.4)	-2.3 (-2.3)
Imports of services	1.9	2.0	0.3 (1.1)	-0.7 (-1.1)	2.6 (1.7)	5.5 (3.7)	-0.8 (-5.0)	5.0 (4.8)
<b>Gross Domestic Product</b>	<b>1.5</b>	<b>2.9</b>	<b>2.9</b> <b>(0.5)</b>	<b>3.0</b> <b>(0.5)</b>	<b>3.0</b> <b>(0.8)</b>	<b>2.9</b> <b>(0.9)</b>	<b>2.6</b> <b>(0.3)</b>	<b>1.8</b> <b>(-0.1)</b>
<i>Change in the main price indicators (%)</i>								
<b>GDP deflator</b>	<b>3.7</b>	<b>1.4</b>	<b>1.8</b> <b>(-0.7)</b>	<b>0.6</b> <b>(*)</b>	<b>1.6</b> <b>(1.7)</b>	<b>1.5</b> <b>(0.5)</b>	<b>2.2</b> <b>(0.1)</b>	<b>3.5</b> <b>(1.4)</b>
<b>Composite CPI</b>								
<b>Headline</b>	<b>4.1</b>	<b>4.3</b>	<b>3.7</b> <b>(1.1)</b>	<b>4.0</b> <b>(1.3)</b>	<b>5.3</b> <b>(-0.8)</b>	<b>4.3</b> <b>(2.7)</b>	<b>4.2</b> <b>(1.0)</b>	<b>3.6</b> <b>(0.7)</b>
<b>Underlying<sup>^</sup></b>	<b>4.7</b>	<b>4.0</b>	<b>3.8</b> <b>(1.1)</b>	<b>3.9</b> <b>(1.1)</b>	<b>4.3</b> <b>(0.8)</b>	<b>4.0</b> <b>(1.0)</b>	<b>3.8</b> <b>(0.9)</b>	<b>3.5</b> <b>(0.7)</b>
<b>Change in nominal GDP (%)</b>	<b>5.3</b>	<b>4.3</b>	<b>4.8</b>	<b>3.6</b>	<b>4.6</b>	<b>4.4</b>	<b>4.8</b>	<b>5.4</b>

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.

(<sup>^</sup>) After netting out the effects of Government's one-off relief measures.

(\*) Change of less than 0.05%.



**Table 2****Economic forecasts for 2014  
(rate of change (%))**

	Forecasts for 2014 as released <u>on 16.5.2014</u> (%)	Latest forecasts for 2014 <u>on 15.8.2014</u> (%)
<b>Gross Domestic Product (GDP)</b>		
<i>Real GDP</i>	3 to 4	<i>2 to 3</i>
<i>Nominal GDP</i>	4 to 5	<i>4 to 5</i>
<b>Composite Consumer Price Index (CCPI)</b>		
<i>Headline CCPI</i>	4.6	<i>4.4</i>
<i>Underlying CCPI</i>	3.7	<i>3.5</i>