Press Release

(embargoed until 4:30 p.m. on 13 May 2016)

Economic Situation in the First Quarter of 2016 and Latest GDP and Price Forecasts for 2016

The Government released today (13 May) the First Quarter Economic Report 2016, together with the preliminary figures on Gross Domestic Product (GDP) for the first quarter of 2016.

The Principal Economist, Mr Andrew Au, described the economic situation in the first quarter of 2016 and provided the latest GDP and price forecasts for 2016.

Main points

* The Hong Kong economy slowed further in the first quarter of 2016, growing meagrely by 0.8% in real terms over a year earlier. This compared to the 1.9% growth in the preceding quarter. The external environment deteriorated during the quarter, characterised by subdued global growth and sharp gyrations in global financial and monetary conditions, leading to a deeper setback in both goods and services trade. The domestic sector also lost some momentum, as the weak global outlook with rising downside risks affected local economic sentiment. On a seasonally adjusted quarter-to-quarter comparison, real GDP fell by 0.4% in the first quarter, after a 0.2% growth in the preceding quarter.

* Strong headwinds in the external environment persisted in the first quarter, weighing heavily on global trade flows. Many advanced economies were still in a fragile state and their persistently sluggish import demand took a heavy toll on Asia's production and trading activities. Heightened financial market volatility and the uncertainty arising from the monetary policy actions by major central banks also added downward pressures. Against this background, Hong Kong's total exports of goods deteriorated further in the first quarter, down by 3.6% in real terms from a year earlier. Exports of services remained in the doldrums, with a year-on-year decline of 4.9%, inflicted by a sharper drop in visitor arrivals and weaker visitor spending, and by sluggish cargo and trade flows.

* While the domestic segment exhibited remarkable resilience last year, the prolonged weakness in the external sector, austere global economic environment, and recent asset market corrections, all sapped economic sentiment, pulling in the reins on domestic demand. Private consumption expenditure slowed visibly from the preceding quarter, growing only mildly by 1.1% year-on-year in real terms in the first quarter. This, together with the continued slowdown in inbound tourism, posed a severe drag on retail sales, which saw the largest year-on-year decline since the Asian financial crisis in 1998. Meanwhile, investment expenditure extended the decline, falling by 10.1% over a year earlier, mainly dragged by the large fall in machinery and equipment acquisition.

* The labour market stayed largely stable in the first quarter, notwithstanding the slowdown in the overall economy, with the seasonally adjusted unemployment rate edging up to a still-low level of 3.4%. Wages and earnings sustained moderate growth. However, total employment grew only slightly and labour demand saw signs of further weakening, particularly in the trade- and tourism-related sectors.

* The local stock market underwent another correction at the start of the year, reflecting increased global financial volatility upon the bleaker global outlook and intensified divergence in monetary policy stances among major central banks. Stock prices have nevertheless rebounded somewhat since mid-February. The residential property market remained quiet during the first quarter, with flat prices still on the decline alongside a visible slowdown in trading activities.

* Looking ahead, global economic growth is likely to remain modest in the near term, with risks still tilted towards the downside. Recoveries in many advanced economies, including Japan and those in the eurozone, are still fragile. Heightened geopolitical tensions and the uncertainty about the potential exit of the UK from the EU have also posed additional challenges. While the global stock markets have rebounded somewhat in the recent months, the situation remains choppy, and the uncertainties associated with the US interest rate normalisation and increasing policy divergence among major central banks could add financial volatility again, posing a threat to the global economy. On the other hand, the US economy, while losing some traction in the first quarter, is expected to show slightly faster growth in the coming quarters. Recent activity indicators suggested that the Mainland economy continued to grow solidly and is on track to attain its growth target of 6.5-7% for the year. In short, the trading environment for Hong Kong's exports, as well as those of other Asian economies, will remain rather difficult in the coming months. Yet, if the economic conditions in our major export markets show improvements going forward, the downward pressures on Hong Kong's exports will hopefully lessen in the latter part of the year. As to Hong Kong's exports of services, the weakness in inbound tourism will continue to pose a drag in the near term, though the pace of decline in visitor arrivals has narrowed somewhat more recently.

* Locally, the package of relief measures in the 2016-17 Budget should render some support to the economy. However, the uncertain global economic outlook and local asset market fluctuations may continue to impinge on economic sentiment. The latest Quarterly Business Tendency Survey also showed that large enterprises have remained rather cautious about the business outlook. The Government needs to stay alert to the repercussions of the slowdown in inbound tourism and slower economic growth on the labour market conditions in the period ahead.

* Taking into account the actual growth outturn in the first quarter and the various external uncertainties still faced by the Hong Kong economy, the forecast real GDP growth of 1-2% for 2016, as announced in the Budget, is maintained in the current round of review.

* Price pressures remained moderate, with underlying consumer price inflation (by reference to the 2014/15-based series) edging up to 2.8% in the first quarter, mainly due to the surge in basic food prices amid bad weather conditions. Given subdued global inflation, and barring significant fluctuations in food and other commodity prices, import prices will likely stay soft. The further retreat in rental inflation amid the property market consolidation, coupled with the slow pace of economic expansion, should keep local cost pressures in check. The forecast rates of underlying and headline consumer price inflation for 2016 as a whole put out in the Budget round, at 2% and 2.3% respectively, are therefore maintained in the current round of review.

Details

GDP

According to the preliminary data on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, GDP grew meagrely by 0.8% in real terms in the first quarter of 2016 over a year earlier, slower than the 1.9% growth in the preceding quarter (same as the earlier estimate). On a seasonally adjusted quarter-to-quarter comparison, real GDP fell by 0.4% in the first quarter, after the 0.2% growth in the preceding quarter (same as the earlier estimate) ***(Chart)***.

2. The latest figures on GDP and its major expenditure components up to the first quarter of 2016 are presented in ***Table 1***. Developments in different segments of the economy in the first quarter of 2016 are described below.

External trade

3. *Total exports of goods* registered a larger year-on-year decline of 3.6% in real terms in the first quarter, after falling by 0.5% in the preceding quarter. The weakness of export performance was actually part of a regional phenomenon, as exports of Asian economies were hard hit by the protracted sluggishness of global demand. Exports to the advanced markets dived further in the first quarter given their fragile economic conditions, while exports to many Asian markets were curbed by subdued intra-regional trade flows. The Indian market was among the few exceptions that still registered notable growth. On a seasonally adjusted quarter-to-quarter basis, total exports of goods fell by 3.9% in real terms in the first quarter, after the 2.3% growth in the preceding quarter.

4. *Exports of services* suffered another setback in the first quarter, down visibly by 4.9% in real terms from a year earlier, after the 2.7% decline in the preceding quarter. Exports of travel services posed a severe drag, amid markedly lower visitor arrivals and weaker visitor spending. Exports of trade-related and transportation services remained battered by subdued trade and cargo flows. Exports of financial and other business services also weakened to decline slightly, as the more volatile global financial and monetary conditions dampened cross-border financial and commercial activities in the quarter. On a seasonally adjusted basis, exports of services declined by 1.8% in real terms in the first quarter over the preceding quarter.

Domestic sector

5. The domestic sector lost some momentum in the first quarter, as the uncertain global economic outlook dented local economic sentiment. The asset market consolidation amid the volatile financial environment also added woes to local consumption demand, partly offsetting the support from the broadly stable labour market conditions. *Private consumption expenditure* continued to moderate in the first quarter, growing only mildly by 1.1% in real terms over a year earlier, down from the 2.7% growth in the preceding quarter. On a seasonally adjusted quarter-to-quarter comparison, private consumption expenditure fell by 0.4% in real terms in the first quarter. *Government consumption expenditure,* on the other hand, grew steadily by 3.2% year-on-year in real terms in the first quarter, providing some cushion to domestic demand.

6. Overall investment spending in terms of *gross domestic fixed capital formation* remained on the downtrend, falling by 10.1% year-on-year in real terms in the first quarter, after the 9.4% plunge in the preceding quarter. Machinery and equipment acquisition was a key drag, plummeting by 11.9% in real terms over a year earlier, conceivably reflecting the scaling back of investment plans amid growing pessimism over the global economic outlook. Overall building and construction activity registered a modest year-on-year decline of 0.8% in real terms, as public infrastructure works decelerated from their peak last year, even though private sector building works still expanded solidly.

The labour sector

7. The labour market was largely stable, with the *seasonally adjusted unemployment rate* edging up by 0.1 percentage point from the preceding quarter to 3.4% in the first quarter. The *underemployment rate* stayed unchanged at 1.4%. Wages and earnings remained on the rise. However, total employment grew only slightly in the first quarter. Moreover, there were further signs of weakening in labour demand, particularly in the trade- and tourism-related sectors, reflecting the lustreless external trade, the protracted slowdown in inbound tourism and the growth moderation in private consumption.

The asset markets

8. The *local stock market* underwent another correction at the start of 2016, as increasing worries over a slowing global economy and wider monetary policy divergence heightened global financial volatility, triggering a new round of global stock market rout and massive sell-offs. The Hang Seng Index (HSI) came under pressure on entering 2016 and hit a low of 18 320 at the close of 12 February, before rebounding somewhat. The HSI closed at 19 915 on 12 May, 9.1% lower than at end-2015.

9. The *residential property market* remained in the consolidation mode in the first quarter. Trading volume tumbled by 39% from the preceding quarter. Residential property prices shed another 5% between December 2015 and March 2016, cumulating to a 12% decline from the peak in 2015. Notwithstanding the recent consolidation, overall flat prices in March 2016 still exceeded the 1997 peak by 56%, and the housing affordability ratio remained elevated at around 59% in the first quarter. Similarly, flat and shop rentals went lower by 5% and 2% respectively during the first quarter, while office rentals were little changed.

Prices

10. Consumer price inflation stayed moderate alongside the continued subpar performance of the overall economy. By reference to the new 2014/15-based series and netting out the effects of the Government’s one-off relief measures, *underlying consumer price inflation* went up slightly to 2.8% in the first quarter, from 2.2% in the preceding quarter (or from 2.4% to 2.9% by reference to the old 2009/10-based series). The slight pick-up in the underlying inflation in the first quarter was mainly driven by the surge in basic food prices amid bad weather conditions. This factor aside, domestic price pressures generally remained in check, given the weaker consumption demand and the easing rental inflation in tandem with the property market consolidation. Meanwhile, external price pressures were muted, thanks to the rather benign inflation in Hong Kong’s major import partners and the still-low international commodity prices. *Headline consumer price inflation* also went up modestly to 2.8% in the first quarter, from 2.3% in the preceding quarter (or from 2.4% to 2.9% by reference to the old 2009/10-based series).

Latest GDP and price forecasts for 2016

11. Looking ahead, global economic growth is likely to remain modest in the near term, with risks still tilted towards the downside. Recoveries in many advanced economies, including Japan and those in the eurozone, are still fragile. Heightened geopolitical tensions and the uncertainty about the potential exit of the UK from the EU have also posed additional challenges. While the global stock markets have rebounded somewhat in the recent months, the situation remains choppy, and the uncertainties associated with the US interest rate normalisation and

increasing policy divergence among major central banks could add financial volatility again, posing a threat to the global economy. On the other hand, the US economy, while losing some traction in the first quarter, is expected to show slightly faster growth in the coming quarters. Recent activity indicators suggested that the Mainland economy continued to grow solidly and is on track to attain its growth target of 6.5-7% for the year. In short, the trading environment for Hong Kong's exports, as well as those of other Asian economies, will remain rather difficult in the coming months. Yet, if the economic conditions in our major export markets show improvements going forward, the downward pressures on Hong Kong's exports will hopefully lessen in the latter part of the year. As to Hong Kong's exports of services, the weakness in inbound tourism will continue to pose a drag in the near term, though the pace of decline in visitor arrivals has narrowed somewhat more recently.

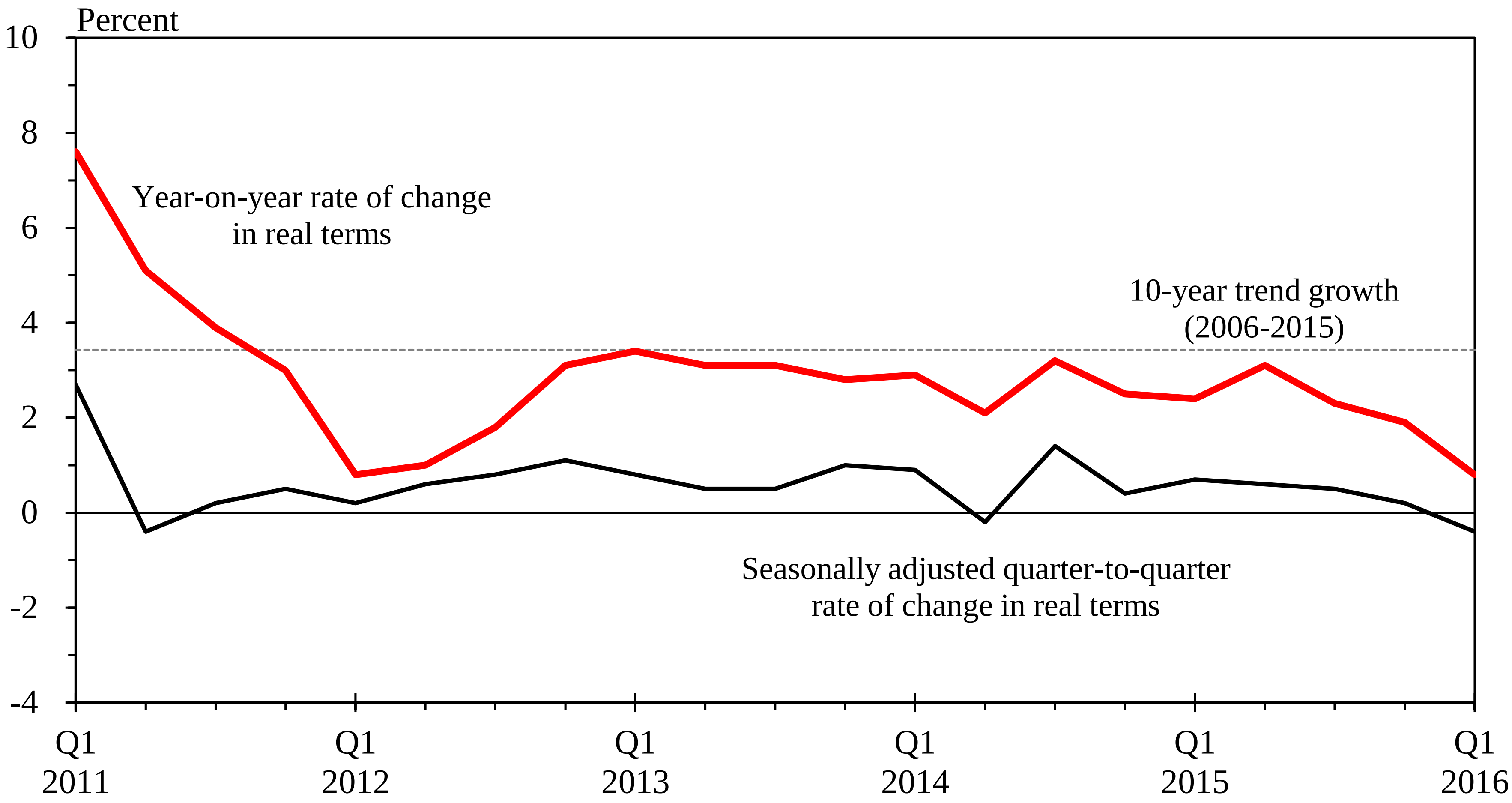
12. Locally, the package of relief measures in the 2016-17 Budget should render some support to the economy. However, the uncertain global economic outlook and local asset market fluctuations may continue to impinge on economic sentiment. The latest Quarterly Business Tendency Survey also showed that large enterprises have remained rather cautious about the business outlook. The Government needs to stay alert to the repercussions of the slowdown in inbound tourism and slower economic growth on the labour market conditions in the period ahead.

13. Taking into account the actual growth outturn in the first quarter and the various external uncertainties still faced by the Hong Kong economy, the forecast real GDP growth of 1-2% for 2016, as announced in the Budget, is maintained in the current round of review ***(Table 2)***. For reference, the latest forecasts by private sector analysts mostly range from 1.0-2.6%, averaging around 1.7%.

14. On inflation outlook, the upside risks to inflation should remain contained in the near term. Given subdued global inflation, and barring significant fluctuations in food and other commodity prices, import prices will likely stay soft. The further retreat in rental inflation amid the property market consolidation, coupled with the slow pace of economic expansion, should keep local cost pressures in check. The forecast rates of underlying and headline consumer price inflation for 2016 as a whole put out in the Budget round, at 2% and 2.3% respectively, are therefore maintained in the current round of review ***(Table 2)***.

(The First Quarter Economic Report 2016 is now available for online download, free of charge at www.hkeconomy.gov.hk/en/reports/index.htm. The Report of the Gross Domestic Product, First Quarter 2016, which contains the GDP figures up to the first quarter of 2016, is also available for online download, free of charge at the homepage of the Census and Statistics Department, www.censtatd.gov.hk.)

Hong Kong's Gross Domestic Product



Note : Figures for the first quarter of 2016 are preliminary estimates.

Table 1

Gross Domestic Product, its main expenditure components and the main price indicators (year-on-year rate of change (%))

	2014#	2015#	2015 Q1#	2015 Q2#	2015 Q3#	2015 Q4#	2016 Q1+
Change in real terms of GDP and its main expenditure components (%)							
Private consumption expenditure	3.3	4.7	5.0 (1.3)	6.8 (1.6)	4.4 (*)	2.7 (-0.1)	1.1 (-0.4)
Government consumption expenditure	3.0	3.4	3.9 (1.0)	3.6 (0.8)	2.8 (0.5)	3.3 (1.0)	3.2 (0.9)
Gross domestic fixed capital formation	-0.1	-2.0	5.6	3.9	-6.2	-9.4	-10.1
of which :							
Building and construction	9.3	2.9	-3.9	14.1	4.2	-0.9	-0.8
Machinery, equipment and intellectual property products	-8.6	-5.8	10.4	-4.7	-10.7	-12.9	-11.9
Total exports of goods	0.8	-1.9	0.2 (-1.9)	-3.8 (-2.4)	-3.1 (0.5)	-0.5 (2.3)	-3.6 (-3.9)
Imports of goods	0.9	-2.7	-0.2 (-2.6)	-3.3 (-2.4)	-4.2 (-0.8)	-2.8 (2.0)	-5.4 (-4.2)
Exports of services	1.1	-0.2	0.7 (0.6)	1.6 (-0.8)	-0.2 (-1.1)	-2.7 (-1.4)	-4.9 (-1.8)
Imports of services	1.8	5.7	6.7 (1.8)	5.1 (1.9)	5.5 (0.2)	5.4 (1.4)	3.8 (0.3)
Gross Domestic Product	**2.7**	**2.4**	**2.4 (0.7)**	**3.1 (0.6)**	**2.3 (0.5)**	**1.9 (0.2)**	**0.8 (-0.4)**
Change in the main price indicators (%)							
GDP deflator	**2.9**	**3.6**	**4.3 (1.2)**	**4.2 (1.0)**	**3.4 (0.1)**	**2.8 (0.4)**	**2.3 (0.7)**
Composite CPI							
Headline	**4.4**	**3.0@**	**4.4 (0.3)@**	**3.0 (-0.6)@**	**2.3 (-0.1)@**	**2.3@ (2.7)@**	**2.8@ (0.7)@**
Underlying^	**3.5**	**2.5@**	**2.7 (0.3)@**	**2.5 (0.6)@**	**2.4 (0.5)@**	**2.2@ (0.9)@**	**2.8@ (0.7)@**
Change in **nominal GDP** *(%)*	**5.6**	**6.2**	**6.8**	**7.5**	**5.8**	**4.8**	**3.1**

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.
(^) After netting out the effects of Government's one-off relief measures.
(*) Change within ± 0.05%.
(@) By reference to the new 2014/15-based CPI series.

Table 2

Economic forecasts for 2016
(rate of change (%))

	Forecasts as released on 24.2.2016 (%)	Latest forecasts on 13.5.2016 (%)
Real Gross Domestic Product (GDP)	1 to 2	*1 to 2*
Composite Consumer Price Index (CCPI)		
Underlying CCPI	2	*2*
Headline CCPI	2.3	*2.3*