

Medium-term outlook for the Hong Kong economy

2.27 Over the medium term, the outlook for the Hong Kong economy remains positive, though external uncertainties still abound on the economic, political and policy fronts. Global economic growth will likely stay modest for an extended period under the “new normal” with unresolved structural issues, while new risks have emerged.

2.28 Among the advanced economies, the US economic outlook is more promising, but will hinge on whether the intended effects of the new US administration’s growth-enhancing policies will be materialised, and how they may affect the Fed’s course of interest rate normalisation and global growth prospects. Meanwhile, many economies in the euro area and Japan are still troubled by lingering structural problems. Apart from the lack of clarity about the trade policy direction of the US, the unfolding of Brexit could also affect future developments in global trade and investment flows. The negotiation process between the UK and the EU is likely to extend beyond 2017. Whether anti-globalisation and protectionist sentiments will spread and result in a change towards more inward-oriented policies in the major economies in the coming years warrant a close watch. Moreover, the potential output growth of many advanced economies beyond the near term looks set to slow amid the absence of a strong demand-side recovery, a protracted period of underinvestment, a slowdown in productivity growth and the intensification of population ageing over time.

2.29 Emerging market economies, in contrast, will remain the main propellers of global economic growth over the medium term. Many emerging market economies have devoted considerable efforts to reduce vulnerabilities and enhance resilience against external shocks, and this should hopefully bear fruit. In particular, Asian economies will likely continue to shine in the global economic arena, underpinned by their stronger economic fundamentals and resilient domestic demand.

2.30 Given Asia’s rising prominence in the global economy, strengthening economic co-operation with the Mainland and our neighbouring economies is vital to Hong Kong’s economic development over the longer run. The Mainland’s economic reorientation towards domestic consumption and the services sector and a further opening up of its market will likely raise the demand for Hong Kong’s higher-end services, especially in the areas of finance and professional services. Closer linkages with the Mainland’s financial markets, the internationalisation of the RMB, the “going-out” of Mainland

enterprises, as well as the Belt and Road Initiative, will continue to bring forth extensive opportunities, enabling Hong Kong to serve as a fund-raising and financial management platform, a trade and logistics hub, as well as an investment springboard. CEPA and other co-operation platforms will help deepen our economic integration with the Mainland and consolidate our status as the world's leading offshore RMB business centre and premier asset management hub. Separately, the Government will strive to explore ways to expand trade and investment flows with neighbouring economies and emerging markets that have promising growth prospects.

2.31 In order to make Hong Kong stand out in the midst of the intense global competition, the Government has made continuous efforts to promote Hong Kong's transformation into a high value-added and knowledge-based economy. The Government will further enhance the competitiveness of our pillar industries and promote new growth areas, including riding on the global wave of Fintech and the applications of other innovative technologies. The Government is also committed to raising productivity growth and uplifting our competitiveness through improving the quality of human and physical capital.

2.32 Hong Kong has long been a staunch supporter of free trade, achieving remarkable economic success by leveraging on the opportunities arising from globalisation over the past decades. In face of lingering external uncertainties, the Government will continue to uphold institutional strengths and to make the most out of the free market mechanism, which form the cornerstone of our economy. These include an open market with free movement of goods, capital and people, a low and simple tax regime, a level-playing field for all businesses, the rule of law, an independent judiciary, and the protection of intellectual property rights. All these important institutions will continue to support a favourable business environment for attracting companies, start-ups and entrepreneurs from overseas and the Mainland to invest and expand their business activities in Hong Kong.

2.33 Meanwhile, population ageing, a common phenomenon across advanced economies, has become a more visible challenge to Hong Kong's economic growth, as the labour force could peak as early as in 2018. In response to an ageing population, the Government has adopted a multi-pronged approach by encouraging labour force participation, enhancing the quality of workforce through education and training, attracting talent from outside Hong Kong and creating a family- and age-friendly environment. An ageing society will have profound impacts on public expenses, particularly in the areas of healthcare and social welfare. Yet, the Government will strive to maintain the

health of our public finances such that sufficient public resources can be ensured to foster economic development and to build an inclusive society, through tackling the various needs of our economy, including investments in education, training and infrastructure for raising productivity growth, and addressing social issues through different programmes. Taking into account the developments on the external and domestic fronts, the economy is expected to attain a trend growth of 3% per annum in real terms from 2018 to 2021.

2.34 Inflationary pressures are expected to remain moderate over the medium term. Externally, modest global economic growth will likely keep world inflation at a relatively low level. Locally, productivity gains should play a part in alleviating some of the local cost pressures. The Government's incessant efforts to increase land and housing supply will improve the demand-supply situation in the property market, helping to contain rental cost pressures in the years ahead. Taking all these developments into account, the trend rate of change in the underlying Composite CPI in Hong Kong from 2018 to 2021 is forecast at 2.5% per annum. There are, however, upside risks to Hong Kong's inflation outlook, if international food and energy prices accelerate sharply due to adverse supply shocks, or if the global economic recovery is stronger than expected and leads to more rapid increases in inflationary pressures.

Diagram 2.14 : Medium-term trend growth forecast at 3% per annum

