

Press Release

(embargoed until 4:30 p.m. on 16 November 2018)

Economic Situation in the Third Quarter of 2018 and Latest GDP and Price Forecasts for 2018

The Government released today (16 November) the Third Quarter Economic Report 2018, together with the preliminary figures on Gross Domestic Product (GDP) for the third quarter of 2018.

The Government Economist, Mr Andrew Au, described the economic situation in the third quarter of 2018 and provided the latest GDP and price forecasts for 2018.

Main points

- * The Hong Kong economy grew solidly by 2.9% in the third quarter of 2018 over a year earlier. While marking the eighth consecutive quarter of above-trend growth, it moderated from the 3.5% growth in the second quarter. External demand continued to record visible growth for the quarter as a whole alongside further expansion of the global economy. Domestic demand held firm. Labour market conditions remained favourable, while consumer price inflation went up slightly. On a seasonally adjusted quarter-to-quarter comparison, real GDP grew by 0.1% in the third quarter of 2018, having decreased by 0.2% in the preceding quarter.
- * Total exports of goods sustained further notable growth of 5.0% year-on-year in real terms for the third quarter as a whole, with most major markets showing growth of varying degrees. Yet the pace of export growth decelerated in September, as the impact of the US-Mainland trade conflicts began to surface. Exports of services expanded moderately by 3.1% in the third quarter. Underpinned by visible expansion in inbound tourism, exports of travel services grew solidly, albeit at a decelerated rate. Amid the heightened external uncertainties and slower momentum of cross-border financial activities, growth in exports of financial services moderated, while exports of transport services, and business and other services recorded only modest increases.
- * Domestic demand stayed largely resilient in the third quarter. Private consumption expenditure, albeit less buoyant than in the previous quarters, expanded notably by 5.2% year-on-year in real terms, buttressed by favourable job and income conditions. Overall investment expenditure picked up significantly to grow by 8.2%, as machinery and equipment acquisition surged and building and construction activity registered a narrower decline.
- * The labour market remained tight in the third quarter. The seasonally adjusted unemployment rate stayed unchanged at a 20-year low of 2.8%, while the underemployment rate edged up to a still-low level of 1.2%. Total employment sustained visible growth on a year-on-year basis. Wages and earnings also registered solid and broad-based gains in real terms.

- * The local stock market saw further consolidation in the third quarter, as the increased external headwinds weighed on market sentiment. The residential property market showed some cool-off, with flat prices switching to fall amid shrinking transactions.
- * Looking ahead, the economic outlook is subject to increasing downside risks. The global economy has lost some momentum of late, as evidenced by the slower growth in the EU and in many Asian economies in the third quarter. The US-Mainland trade conflicts have weighed on global economic sentiment, with possible repercussions on global trade and investment activities. The impacts on Hong Kong's external trade have begun to surface, and are likely to become more apparent in the near term. The further tightening of financial conditions across advanced economies, particularly in the US, is another risk factor. The US Federal Reserve has hiked interest rate three times this year, and signalled further gradual rate hikes going forward. Rising US interest rates and a stronger US dollar had already wreaked financial havoc in some emerging market economies with weak fundamentals earlier this year. Global financial and asset markets could become even more volatile in the period ahead. Besides, developments related to Brexit, Italy's fiscal situation and geopolitical tensions also warrant close attention.
- * Domestic demand may also be subject to more pressure from the rising external headwinds. Consumer sentiment, while still being supported by the favourable job and income conditions, could increasingly be affected by the external uncertainties and weaker asset markets. Various surveys also revealed that local business sentiment has become more cautious in recent months.
- * Taking into account the actual growth outturn of 3.7% in the first three quarters of 2018 and the downside risks in the external environment, economic growth for 2018 as a whole is now forecast at 3.2%, within the range forecast of 3-4% announced in the August round. The Government will continue to monitor closely the external and domestic developments, for their possible impacts on the economic and employment situations.
- * Pressures on consumer prices continued to build up alongside sustained above-trend economic growth. The underlying consumer price inflation picked up to 2.8% in the third quarter, averaging 2.5% for the first three quarters as a whole. Looking ahead, the inflation rate may still be subject to some mild upward pressure in the rest of the year, as local costs have increased along with the sustained economic expansion, and as the earlier rises in fresh-letting residential rentals would continue to feed through. Taking into account the actual outturns so far this year, the forecast rates of underlying and headline consumer price inflation for 2018 as a whole are slightly revised upwards to 2.7% and 2.4% respectively in the current round of review, from 2.5% and 2.2% in the August round.

Details

GDP

According to the preliminary data on the *Gross Domestic Product (GDP)* released today by the Census and Statistics Department, GDP grew solidly by 2.9% in real terms in the third quarter of 2018 over a year earlier. While marking the eighth consecutive quarter of growth above the trend growth rate of 2.7% per annum in the past ten years, it moderated from the 3.5% growth in the second quarter (same as the preliminary estimate). On a seasonally adjusted quarter-to-quarter comparison, real GDP grew by 0.1% in the third quarter of 2018, having decreased by 0.2% in the preceding quarter (same as the preliminary estimate) (*Chart*).

2. The figures on GDP and its major expenditure components up to the third quarter of 2018 are presented in *Table 1*. Developments in different segments of the economy in the third quarter of 2018 are described below.

External trade

3. *Total exports of goods* grew notably by 5.0% in real terms in the third quarter over a year earlier, after a similar 4.6% growth in the second quarter. However, external merchandise trade statistics showed that export growth decelerated visibly in September, suggesting that the impacts of the US-Mainland trade conflicts have begun to surface. For the third quarter as a whole, exports to most major markets showed growth of varying degrees. Exports to the US grew visibly, underpinned by a pick-up in import demand alongside strong economic expansion there. While those re-exports of Mainland origin to the US affected by the additional tariffs imposed in July and August showed notable deceleration in August and September, they constituted only about 15% of Hong Kong's total exports to this market in the third quarter. As to exports to the EU, visible growth was also recorded amid sustained economic growth in the region. Exports to most major Asian markets also grew by varying extents alongside further expansion in intra-regional trade. Specifically, exports to the Mainland continued to grow visibly. Exports to India and major emerging markets in ASEAN posted discernible growth. As to the high-income Asian markets, exports to Korea picked up, and those to Singapore saw still-solid growth, but those to Japan and Taiwan registered declines. On a seasonally adjusted quarter-to-quarter basis, total exports of goods increased by 1.2% in real terms in the third quarter, having decreased by 0.4% in the second quarter.

4. *Exports of services* expanded moderately by 3.1% year-on-year in real terms in the third quarter, after a 5.9% growth in the preceding quarter. Underpinned by visible expansion in inbound tourism, exports of travel services grew solidly, albeit at a decelerated rate. Amid the heightened external uncertainties and slower momentum of cross-border financial activities, growth in exports of financial services moderated, while exports of transport services, and business and other services recorded only modest increases. On a seasonally

adjusted quarter-to-quarter basis, exports of services increased by 0.1% in real terms in the third quarter, having declined by 3.3% in the preceding quarter.

Domestic sector

5. Domestic demand remained largely resilient in the third quarter. *Private consumption expenditure* expanded notably by 5.2% in real terms over a year earlier, albeit moderated somewhat from the exceptionally strong growth of 7.4% in the first half of the year. Local consumer sentiment continued to be buttressed by favourable job and income conditions, though the wealth effect may have turned less supportive amid the stock market corrections. On a seasonally adjusted quarter-to-quarter comparison, private consumption expenditure increased by 0.9% in real terms in the third quarter, after the decrease of 0.7% in the preceding quarter. *Government consumption expenditure* grew steadily by 3.3% in real terms in the third quarter over a year earlier, following the 4.3% growth in the preceding quarter.

6. Overall investment spending in terms of *gross domestic fixed capital formation* recorded a much faster year-on-year growth of 8.2% in real terms in the third quarter, compared with the 1.1% increase in the second quarter. Within the total, machinery and equipment acquisition, which is usually volatile, surged from a low base of comparison in the same quarter last year. However, local business sentiment has become more cautious in recent months owing to the increased headwinds in the external environment. Meanwhile, overall building and construction activity registered a narrower year-on-year decline.

The labour sector

7. The labour market remained tight in the third quarter. The *seasonally adjusted unemployment rate* stayed unchanged at a 20-year low of 2.8%, while the *underemployment rate* edged up to a still-low level of 1.2%. Total employment registered further visible growth on a year-on-year basis. Against this backdrop, wages and earnings sustained solid and broad-based growth in real terms. Earnings of grassroots workers also stayed on the rise after discounting inflation.

The asset markets

8. The *local stock market* consolidated further in the third quarter, as market sentiment was hit by escalating US-Mainland trade conflicts and successive US rate hikes. The Hang Seng Index closed the third quarter at 27 789, down by 4.0% from a quarter earlier. On 15 November, the Hang Seng Index closed at 26 103.

9. The *residential property market* showed some cool-off. The number of residential property transactions fell by 24% from 18 900 in the second quarter to 14 400 in the third quarter. Overall flat prices edged down by 1% during the third quarter, with the month-to-month increase in July more than offset by declines in August and September. Notwithstanding the latest declines, prices in September

were still higher than the 1997 peak by 125%. Meanwhile, the index of home purchase affordability stayed elevated at around 74% in the third quarter. Between June and September, flat rentals rose further by 2%. Over the same period, shop and office prices increased by 2% and 6% respectively, and their rentals also increased, by 2% and 1% respectively.

Prices

10. Alongside the sustained above-trend economic growth, pressures on consumer prices continued to build up in the third quarter. Domestically, the rises in fresh-letting residential rentals over the past year or so continued to feed through to consumer price inflation. Local cost pressures on factor inputs, while still largely contained, have turned more visible. While wages and earnings continued to register solid gains, rental pressures faced by businesses, albeit broadly moderate, edged up against the broad uptrend in rentals of retail premises and offices. Meanwhile, external price pressures largely held steady. Against this backdrop, the *underlying consumer price inflation*, which nets out the effects of the Government's one-off relief measures, averaged 2.8% in the third quarter, up from 2.4% in the second quarter. *Headline consumer price inflation* also went up to 2.5% from 2.1% over the same period.

Latest GDP and price forecasts for 2018

11. Looking ahead, the economic outlook is subject to increasing downside risks. The global economy has lost some momentum of late, as evidenced by the slower growth in the EU and in many Asian economies in the third quarter. The US-Mainland trade conflicts have weighed on global economic sentiment, with possible repercussions on global trade and investment activities. The impacts on Hong Kong's external trade have begun to surface, and are likely to become more apparent in the near term. The further tightening of financial conditions across advanced economies, particularly in the US, is another risk factor. The US Federal Reserve has hiked interest rate three times this year, and signalled further gradual rate hikes going forward. Rising US interest rates and a stronger US dollar had already wreaked financial havoc in some emerging market economies with weak fundamentals earlier this year. Global financial and asset markets could become even more volatile in the period ahead. Besides, developments related to Brexit, Italy's fiscal situation and geopolitical tensions also warrant close attention.

12. Domestic demand may also be subject to more pressure from the rising external headwinds. Consumer sentiment, while still being supported by the favourable job and income conditions, could increasingly be affected by the external uncertainties and weaker asset markets. Various surveys also revealed that local business sentiment has become more cautious in recent months.

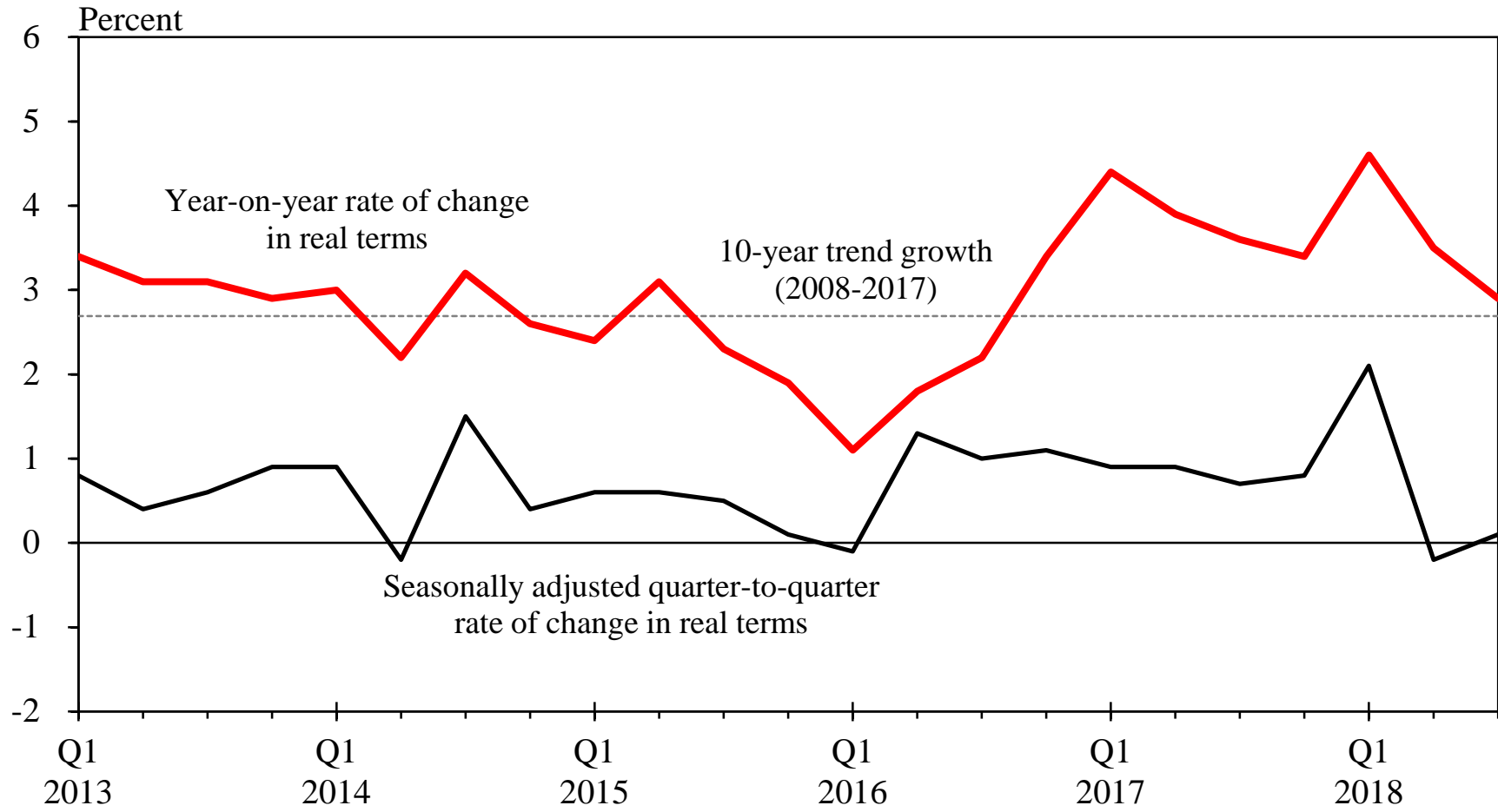
13. Taking into account the actual growth outturn of 3.7% in the first three quarters of 2018 and the downside risks in the external environment, economic growth for 2018 as a whole is now forecast at 3.2%, within the range forecast of

3-4% announced in the August round (*Table 2*). The Government will continue to monitor closely the external and domestic developments, for their possible impacts on the economic and employment situations. For reference, the latest forecasts by private sector analysts range from 3.0-4.0%, averaging around 3.6%.

14. On inflation outlook, the inflation rate may still be subject to some mild upward pressure in the rest of the year, as local costs have increased along with the sustained economic expansion, and as the earlier rises in fresh-letting residential rentals would continue to feed through. Taking into account the actual outturns so far this year, the forecast rates of underlying and headline consumer price inflation for 2018 as a whole are slightly revised upwards to 2.7% and 2.4% respectively in the current round of review, from 2.5% and 2.2% in the August round (*Table 2*).

(The Third Quarter Economic Report 2018 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, Third Quarter 2018, which contains the GDP figures up to the third quarter of 2018, 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 third quarter of 2018 are preliminary estimates.

Table 1

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

	<u>2016[#]</u>	<u>2017[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>2017</u> <u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1[#]</u>	<u>2018</u> <u>Q2[#]</u>	<u>Q3⁺</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>									
Private consumption expenditure	2.0	5.5	3.7 (0.8)	5.8 (2.0)	6.3 (1.8)	6.3 (1.5)	8.8 (3.3)	6.0 (-0.7)	5.2 (0.9)
Government consumption expenditure	3.3	3.4	2.8 (0.6)	3.0 (1.1)	4.5 (1.7)	3.2 (-0.2)	3.9 (1.2)	4.3 (1.5)	3.3 (0.7)
Gross domestic fixed capital formation	-0.1	3.5	5.7	7.6	-2.1	3.1	4.2	1.1	8.2
Building and construction	5.9	1.7	7.0	2.0	0.9	-2.6	1.9	-1.6	-0.3
Costs of ownership transfer	-2.9	22.3	77.8	53.0	-12.8	6.2	11.9	0.7	-1.0
Machinery, equipment and intellectual property products	-6.3	1.8	-7.8	6.1	-3.0	9.9	6.1	4.9	21.2
Total exports of goods ^{&}	1.6	5.9	9.6 (1.2)	5.7 (0.1)	5.7 (0.8)	3.4 (1.1)	5.2 (3.1)	4.6 (-0.4)	5.0 (1.2)
Imports of goods ^{&}	0.7	7.0	10.3 (0.8)	6.4 (0.4)	6.3 (1.5)	5.4 (2.4)	6.9 (2.3)	6.3 (-0.1)	7.6 (2.7)
Exports of services ^{&}	-3.5	3.2	3.3 (1.2)	1.9 (-1.6)	3.5 (3.0)	3.9 (1.2)	7.9 (5.2)	5.9 (-3.3)	3.1 (0.1)
Imports of services ^{&}	2.0	1.9	0.9 (0.2)	4.8 (1.6)	1.4 (-1.7)	0.8 (0.8)	4.2 (3.6)	-0.1 (-2.5)	3.4 (1.8)
Gross Domestic Product	2.2	3.8	4.4 (0.9)	3.9 (0.9)	3.6 (0.7)	3.4 (0.8)	4.6 (2.1)	3.5 (-0.2)	2.9 (0.1)
<i>Change in the main price indicators (%)</i>									
GDP deflator	1.7	2.9	2.4 (0.9)	3.4 (1.1)	3.2 (0.3)	2.8 (0.5)	4.1 (2.1)	4.0 (1.0)	3.7 (0.2)
Composite CPI									
Headline	2.4	1.5	0.5 (0.1)	2.0 (0.6)	1.8 (0.3)	1.6 (0.6)	2.4 (0.9)	2.1 (0.4)	2.5 (0.5)
Underlying[^]	2.3	1.7	1.4 (0.1)	2.0 (0.6)	1.7 (0.3)	1.6 (0.6)	2.4 (0.8)	2.4 (0.8)	2.8 (0.5)
Change in nominal GDP (%)	3.9	6.8	6.8	7.4	6.9	6.3	8.9	7.7	6.7

Notes : Figures are subject to revision later on as more data become available. The 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.

(&) Figures are compiled based on the change of ownership principle in recording goods sent abroad for processing and merchandising under the standards stipulated in the *System of National Accounts 2008*.

(#) Revised figures.

(+) Preliminary figures.

() Seasonally adjusted quarter-to-quarter rate of change.

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

Table 2**Economic forecasts for 2018
(rate of change (%))**

	<u>Forecasts as released on 10.8.2018</u> (%)	<u>Latest forecasts on 16.11.2018</u> (%)
Real Gross Domestic Product (GDP)	3 to 4	3.2
Composite Consumer Price Index (CCPI)		
<i>Underlying CCPI</i>	2.5	2.7
<i>Headline CCPI</i>	2.2	2.4