

## Box 6.2

### Movement in the GDP deflator

The GDP deflator is a broad measure of changes in overall price level in an economy. Under the expenditure approach for compiling GDP, the GDP deflator aggregates movements in the price deflators for the various expenditure components of GDP, with their current relative shares in GDP as weights.

GDP compiled on this basis is equal to total final expenditure comprising domestic demand (DD) and exports of goods and services (X), less imports of goods and services (M); or symbolically,  $GDP = DD + X - M$ . The movement in the GDP deflator is thus affected by price variations associated with both the domestic demand component (including final consumption expenditures of households and government, and fixed asset investment expenditure) and the external trade component (more specifically, change in export prices relative to that in import prices, or change in the terms of trade).

#### GDP deflator, domestic demand deflator and the terms of trade (rate of change (%))

*Of which:*

	<u>GDP deflator</u>	<u>Domestic demand deflator</u>	<u>Terms of trade*</u>
1997	5.7	4.6	-0.1
1998	0.2	0.5	0.9
1999	-5.8	-2.4	-0.7
2000	-6.2	-5.3	-0.9
2001	-1.9	-2.5	0.5
2002	-3.0	-4.5	1.0
2003	-5.1	-3.8	-1.2

Note : (\*) Here the terms of trade is defined as the ratio of the price deflator for total exports of goods and services to that for total imports of goods and services. This is not the same as the terms of trade shown in paragraph 6.17, which is defined as the ratio of the prices of total exports of goods to the prices of imports of goods only.

The GDP deflator in Hong Kong, having risen in both 1997 and 1998, started to follow a downtrend in 1999. Comparing 2003 with 1998, there was a cumulative decrease of 20%. This was largely attributable to continued easing in the prices of goods and services used locally amidst subdued local demand, as borne out by sustained decline in the domestic demand deflator over the period. Yet in 1999, 2000 and 2003, the GDP deflator fell to a larger extent than the domestic demand deflator. This was due to deterioration in the terms of trade, stemming from a relatively steeper fall in export prices than in import prices amidst keen competition in the world market.

In 2003, the domestic demand deflator went down by 3.8%, as the prices of goods and services for local use continued to drift lower, especially so during the period of SARS impact. The terms of trade also declined, by 1.2%, under the influence of a weak US dollar. In consequence, the GDP deflator fell distinctly, by 5.1%.