

Box 2.1

Impact of high oil prices on the Hong Kong economy

The Hong Kong economy is highly service-oriented and is relatively less energy dependent. Reflecting this, fuel cost accounts for only around 2% of total business cost (or around 4% if labour cost is excluded). As such, the direct impact of soaring oil prices on production cost and disposable household income should be relatively mild in overall terms. Yet the cost impact on the more oil-intensive industries, such as airline, local transport, restaurants, construction and fishery, will be relatively higher.

However, the indirect impact stemming from the trade front is of much more concern to Hong Kong, given Hong Kong's dependence on trade. Sustained high oil prices could dent the growth momentum of the global economy and this would inevitably impinge on Hong Kong's trade growth. An earlier study estimates that a US\$10/barrel permanent increase in oil prices will knock down Hong Kong's GDP growth by 0.6 of a percentage point in the first year of incidence, taking on board both the direct impact on household disposable income, as well as the indirect impact working through the trade front.

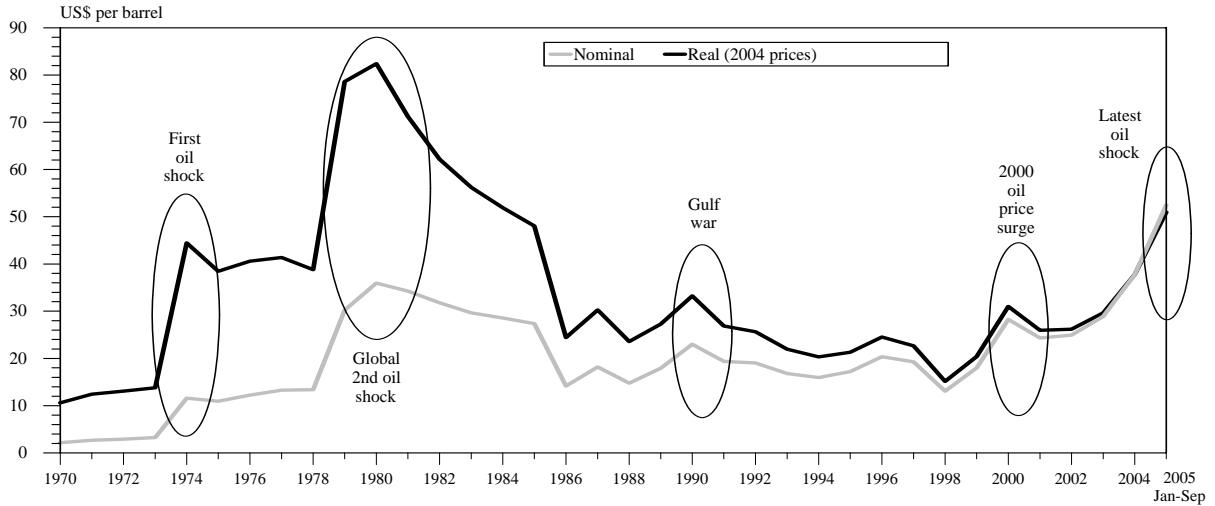
Over the years, fuel usage in Hong Kong has also become increasingly efficient. Hong Kong's primary energy requirements⁽¹⁾ rose by an average annual rate of 1.9% over the past decade, much slower than that of 3.5% of the real GDP growth. Also, Hong Kong is not particularly dependent on oil as a source of primary energy requirements. Overall, about 49% of Hong Kong's primary energy needs come from oil products. More than half of the electricity generated in Hong Kong comes from coal. In addition, Hong Kong has a very efficient public transport system that is heavily used. Hong Kong imposes relatively high taxes on the use of private motor vehicles and on petrol, thus encouraging the use of energy-efficient public transport.

Thus, with much of Hong Kong's economic activity now geared towards services, and with improved fuel usage efficiency and the use of coal in our electricity generation, the impact of oil price upsurge on Hong Kong's production costs should be much milder now than before. Moreover, with the oil dependency in industrialised economies likewise coming down over the years, the impact of oil price surge on global economic activity should also be relatively less damaging now than before. In fact, the global economy has been rather resilient so far in absorbing the impact of higher oil prices. While the growth pace of the United States, the key driving force of global economic growth, has moderated in 2005 from that in 2004, so far it has been fairly robust. This notwithstanding, the distinct surge in oil prices over the past two years is still a key risk that could potentially impinge on global economic activity in the period ahead, with more of the negative impact likely to show up in late 2005 and 2006.

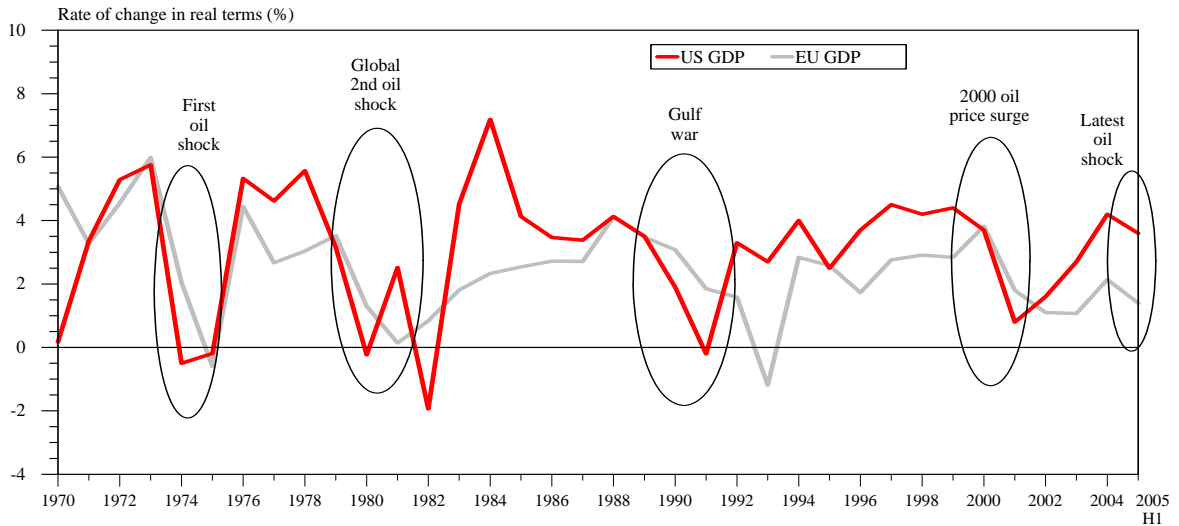
For an analysis of the impact of high oil prices on consumer price inflation, see **Box 6.1** in Chapter 6.

(1): "Primary energy requirements" refer to the overall energy consumption within a geographic territory. It represents the total supply of energy available to the territory, which supports all the requirements for energy transformation and final consumption in that territory. In general, primary energy requirements of a territory include both its indigenous energy sources and imported energy commodities consumed within the territory.

Nominal and real crude oil prices, 1970 - 2005



US and EU GDP growth , 1970 - 2005 H1



Hong Kong GDP growth , 1970 - 2005 H1

