

Box 6.1

Impact of oil price hikes on the Composite CPI

Hong Kong's economy is highly service-oriented and not very oil-dependent, with fuel cost accounting for only around 2% of total business operating cost (or around 4% if labour cost is excluded) for the economy as a whole. Yet certain businesses like electricity and gas companies, transport operators, as well as restaurant and hotels, will be more affected by high oil prices due to the higher share of fuel cost in their total operating costs.

Oil price hikes will lead to higher import prices and hence higher retail prices of oil products in Hong Kong. Yet such direct impact on local consumer prices should not be that significant, given that oil products including motor gasoline, LPG, and kerosene have a combined weighting of only 0.89% in the Composite CPI. Specifically, in September 2005, prices of motor gasoline and LPG were 9.8% and 9.1% higher than a year earlier, as against a 46.0% surge in Brent oil price over the same period. Towngas charges, which were also lifted by higher oil price indirectly, were 10.8% higher. They together contributed 0.21 of a percentage point to the 1.6% CCPI inflation in September (0.25 of a percentage point if the fuel cost adjustments by electricity companies, which had been largely mitigated by other rebates/discounts, were also taken into account). For the first nine months of 2005 as a whole, these fuel-related components contributed 0.14 of a percentage point to the 0.9% CCPI inflation so far this year (0.18 if including electricity companies' fuel cost adjustments).

<u>Economic sector</u>	<u>Fuel cost as a proportion of non-labour business operating cost (%)</u>	<u>Impact of a US\$10/barrel increase in world crude oil prices on total business operating cost (% point)</u>
Electricity, gas and water	around 60	around 4
Wholesale, retail and import/export trades, restaurants and hotels	1.5	0.19
<i>Within which :</i>		
Restaurants and hotels	9.6	1.05
Transport, storage and communications	9.5	2.16
Financing, insurance, real estate and business services	4.9	0.08
Community, social and personal services	4.9	0.06
All sectors as a whole	4.3	0.42

Note : (*) By reference to 2003 as the benchmark year. The oil-related import cost content within the fuel cost content shown in this table varies amongst different economic sectors, depending on the type and amount of oil products consumed.

There would also be some indirect or spill-over effects, as business operators pass on part or all of the higher oil cost onto their consumers should the high oil prices sustain for a period of time, and consumer demand continue to improve. Yet in general, as Hong Kong economy is not oil-dependent, the second round or spill-over effects should be rather modest. Moreover, the pass-through of higher oil prices so far had been slightly less than estimated, because part of the cost increases stemming from oil price had been absorbed in the profit margin. Indeed, for most of the local transport services, the price increases had been very modest, at around 1-2% year-to-date. The increase in prices of dining out in local restaurants and hotels had also been rather mild.