

Box 1.2**Oil shocks in the 1970s
and how they had impacted on Hong Kong economy****First oil price shock in 1973-1974**

Between 1973 and 1974, oil prices more than tripled, triggered by production constraints imposed by OPEC. Given the high oil dependency at that time, this led to severe disruptions to world economic activity. World economic growth slowed from 6.8% in 1973 to 2.8% in 1974 and further to 1.9% in 1975. According to the International Monetary Fund (IMF), the surge in oil prices reduced real GDP of advanced economies by about 2.6 percentage points through the direct impact on net trade balance, as a result of higher oil import bill. World real GDP growth rebounded since late 1975 and showed a 5.1% growth in 1976, partly because oil prices tended to stabilise and partly because advanced economies adopted more accommodative monetary and fiscal policies to revive their economies.

As to Hong Kong, real GDP growth slowed drastically from 12.3% in 1973 to 2.3% in 1974 and further to 0.4% in 1975. This was largely caused by the severe contraction in global and regional demand at that time, resulting in a poor performance of Hong Kong's exports. Real GDP recovered strongly in 1976 to a 16.2% growth, thanks to the revival of exports along with the world economic recovery.

Second oil price shock in 1979-1980

Real oil prices doubled in 1979 and rose by a further 5% in 1980 to an average of about US\$82.4 per barrel (2004 prices), this time triggered by the prolonged war between Iran and Iraq. This occurred at a time when the world economy was already moderating. World real GDP growth slowed from 4.6% in 1978 to 3.8% in 1979 and further to 2.3% and 2.1% in 1980 and 1981 respectively.

By contrast, the Hong Kong economy appeared to have weathered the second oil crisis rather well, partly because of the property market bubble that was building up at that time. Real GDP continued to expand strongly with growth exceeding or near double-digit in all the three years from 1979 to 1981. The impact on Hong Kong was not felt until 1982, when the property bubble burst and GDP growth slowed to 3.0%. Again, the adverse impact came also from the trade front. Economic growth rebounded swiftly to 5.9% in 1983 and then further to 9.9% in 1984, along with a better performance of the world economy and a much weaker Hong Kong dollar.

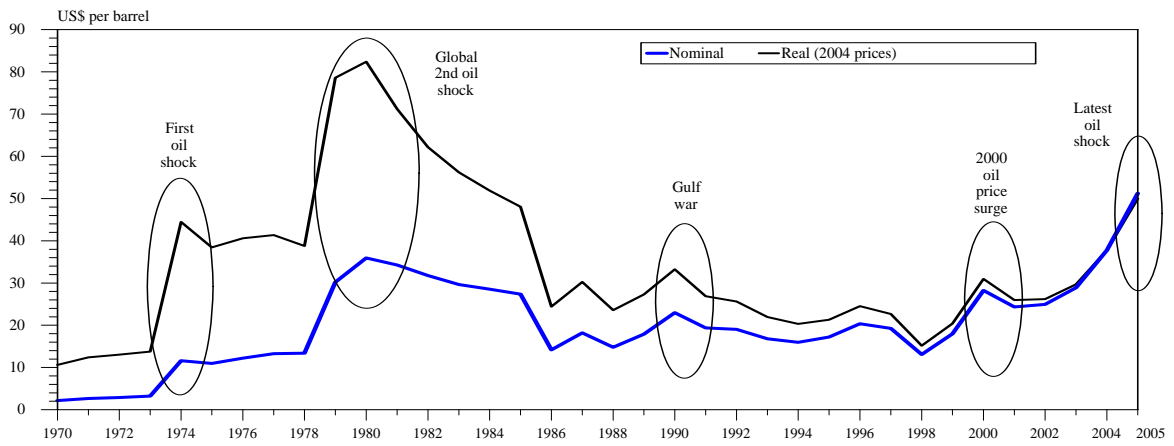
Observations about the oil price shocks in the 1970s

In sum, the first oil price shock in the 1970s resulted in a more significant dampening impact on Hong Kong's economic growth than the second oil price shock did. On both occasions, the adverse impacts on Hong Kong mainly came from the trade front as a result of weakening global demand.

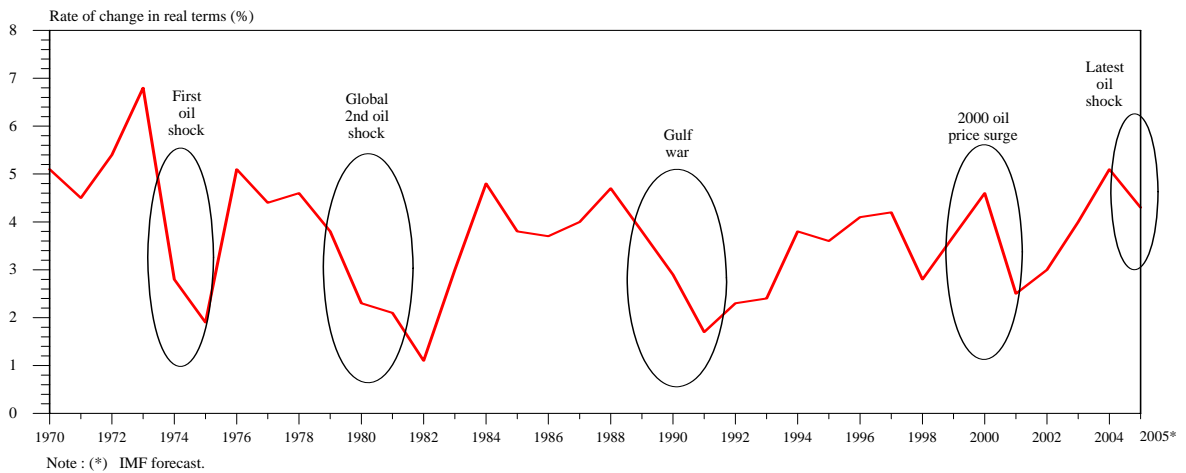
Compared with 30 years ago, the impact of oil price surge on Hong Kong economy should be much milder now. Having gone through the first oil price shock, the Hong Kong economy had adjusted itself to economise on fuel usage, cutting its oil dependency by about one-fourth before the second oil price shock took place. Compared with the early 1970s, by now Hong Kong's oil dependency has come down by some 50%. Also, from the demand side angle, consumers in developed economies, including Hong Kong, now spend more on services than on goods, and the production of consumer services is conceivably less prone to oil price surge than production of goods. Moreover, with globalisation and the substantial improvement in production technology, inflation worldwide has also come down significantly over the past decade, and central banks of the advanced economies are determined to keep inflation in check. All in all, the impact from oil price surge on Hong Kong's economic growth and inflation should be generally less damaging than before.

Box 1.2 (Cont'd)

Nominal and real crude oil prices, 1970 - 2005



World GDP, 1970 - 2005



Hong Kong GDP growth , 1970 - 2005

