Box 5.1

Latest earnings adjustment after the outbreak of the global financial crisis

Hong Kong’s economy has suffered from the increasing impact of global financial and economic crisis since September 2008. Weakening economic activity has depressed the labour demand and hence weighed heavily on labour earnings. Pay reductions have become more noticeable after the Lunar New Year. Many companies decided to engage in staff retrenchment or business restructuring. In the latter case, workers would be shifted to new lines of work, with lower earnings during the adjustment period. To weather the current storm and maintain sustainability of the business, an increasing number of firms in many sectors have requested staff to take unpaid leave. Against the above background, earnings growth for workers has significantly moderated over the past few months.

Relationship between wage inflation and unemployment rate over the short run

The short-run relationship between unemployment and wage growth is portrayed by the short-run Philips Curve. When aggregate demand in the economy exceeds aggregate supply, this will result in an excess demand in the labour market as manifested in a fall in unemployment rate, causing wages to rise as a response to reduce the supply/demand imbalance. Vice versa, when aggregate demand contracts and falls short of aggregate supply, excess supply in the labour market will be manifested in a rise in unemployment rate and will put downward pressure on wages, likewise as a response to reduce the supply glut.

Wage and payroll adjustments over the past decade in Hong Kong

By virtue of its competitiveness and flexibility, on the whole Hong Kong’s labour market has adjusted fairly well through the business cycles in the past 10 years, with unemployment rate moving in tandem with and nominal wages also adjusting in response to the evolving market conditions. During the typical economic downturn, nominal wages would adjust downwards while the less competitive workers are likely to be more vulnerable to job losses. On the other hand, as recovery takes hold, job creation will be more solid and sustained, initially pushing down the unemployment rate and eventually also lifting wage gains. A summary view of the employment situation especially for lower-skilled workers over the past decade is given below (Chart 2 - the zones marked are rough indications for reference only):
Box 5.1 (Cont’d)

Chart 2: Unemployment rate and labour earnings

(a) After being hard hit by the Asian financial crisis in 1997, the overall unemployment rate and that for lower-skilled workers increased steeply afterwards, with notable downward pressure on wage growth during 1998 and early 1999 (Zone A, Chart 2).

(b) During the recovery between mid-1999 and 2000, the overall unemployment rate and that for the lower-skilled workers both fell, with a rebound in wages (Zone B, Chart 2).

(c) The bursting of the dotcom bubble in 2001 and the ensuing outbreak of the Severe Acute Respiratory Syndrome (SARS) in 2003 pushed the overall unemployment rate up to an all-time high of 8.5% in the second quarter of 2003. In parallel, the unemployment rate for lower-skilled workers reached a record high of 10.1% in May – July 2003. Fall in wages was found among most job categories during 2002-2004 (Zone C, Chart 2).

(d) Starting from the second quarter of 2003, unemployment rate began to improve. At the initial recovery stage, more job opportunities emerged for both full-time and part-time workers. However the unemployment rate for lower-skilled workers was still high and corresponding wage rate was still falling, though at a decreasing rate (Zone D1, Chart 2).

(e) As the economic recovery gathered momentum, job creation continued and the overall unemployment rate fell further, while wage increases became more widespread (Zone D2, Chart 2).

(f) With the unemployment rate falling even further amid a booming business environment, employers faced rising labour turnover. More and more firms had to devise ways to retain and train up workers. Wages began to rise across-the-board and the rate of increase accelerated (Zone D3, Chart 2).

(g) The recent global financial and economic crisis has changed the favourable economic landscape for Hong Kong. In view of the increasingly difficult external environment, the local economy is likely to experience a severe contraction in 2009 and the employment situation is expected to worsen with further increase in unemployment rate and moderating wage growth (Zone E, Chart 2). Anecdotal information suggests that a large number of companies have already decided to freeze salaries and some have opted for cutting salaries this year.
Box 5.1 (Cont’d)

Latest employment earnings growth

The latest General Household Survey showed that average year-on-year employment earnings (excluding foreign domestic helpers) declined by 1.6% in November 2008–January 2009 (the first negative growth since December 2004–February 2005), and then further down by 3.6% in the first quarter of 2009.

Since the outbreak of global financial and economic crisis, job losses in the trading and logistics, and financial services (including financing and insurance sectors) sectors have been the most serious, by 29 700 and 13 200 respectively. Significant declines in employment earnings were also found in the related sectors. Employment earnings in the financial services sector fell by 18.7%, mainly reflecting the notable decline (22.1%) for the financing sub-sector (Chart 3). Professional business services ancillary to the financial sector such as accounting services also suffered from notable pay cut. In particular, many accounting firms (including the Big Four) have introduced / announced unpaid leave schemes early this year.

Workers in the logistics sector also registered a reduction in employment earnings of 9.3% (Chart 4). On the external front, the value of Hong Kong’s total merchandise exports tumbled by 22% in the first quarter of 2009. Over the same period, the Mainland’s exports value (which impacts directly on Hong Kong’s re-export trade) fell sharply by 20% over a year earlier. As an indicator of economic activity in the logistics sector, the port of Hong Kong handled 4.5 million TEUs of containers in the first quarter of 2009, representing a year-on-year decline of 21%. Given that the external trade is expected to remain weak, labour demand and earnings growth for workers in the external-oriented sector would continue to be under pressure in the near term.

Near term outlook

In the light of the uncertain economic environment, Hong Kong’s overall unemployment rate is likely to face continuous upward pressure in the near term, while employment earnings would be under further increasing downdrag. The Government is sparing no effort to ease rising unemployment through a multi-pronged strategy and is implementing the series of measures announced earlier to stabilise the financial system, support enterprises, and preserve and create jobs.