

Possible economic losses caused by the local social incidents – An update

Desmond Hou
Principal Economist

Victor Leung
Senior Economist

June 2020

Abstract

The local social incidents involving violent acts in the second half of 2019 caused significant disruptions to inbound tourism and consumption-related economic activities. Based on empirical data, this article crudely estimates the possible economic losses arising from the additional decline in businesses of the retail, restaurant and accommodation sectors, as well as that in other tourists' consumption expenditure due to the incidents. Our crude estimates suggest that these economic losses dragged the year-on-year change in real GDP by more than 2.5 percentage points in the second half of 2019, and were the main reason for the economic recession.

本地社會事件可能導致的經濟損失 – 更新

摘要

2019 年下半年涉及暴力衝擊行為的本地社會事件對訪港旅遊業及與消費相關的經濟活動造成極為沉重的打擊。本文根據客觀數據，粗略推算零售、餐飲和酒店業的業務，以及訪港旅客的其他消費開支可能因有關事件引致的額外跌幅所帶來的經濟損失。根據粗略推算，這些經濟損失對 2019 年下半年實質本地生產總值按年變動的拖累超過 2.5 個百分點，是經濟衰退的主因。

I. INTRODUCTION

1. The local social incidents involving violent acts in the second half of 2019 caused significant disruptions to inbound tourism and consumption-related economic activities. Following the same methodology as adopted in the previous assessment for the third quarter of 2019¹ and based on empirical data, this article crudely estimates the possible economic losses arising from the additional decline in businesses of the retail, restaurant and accommodation sectors, as well as that in other tourists' consumption expenditure due to the incidents in the second half of the year.

II. ESTIMATION METHOD

2. As Hong Kong is a small and open economy, its economic performance is susceptible to external factors. It is not an easy task to conduct a quantitative analysis of the impact of the local social incidents on our economy. We have used several estimation methods and their results are largely consistent. This article elaborates on one of these estimation methods that uses reliable empirical data directly as the basis for estimation. It is also more concise in logical reasoning and yields relatively conservative results.

3. Economic data objectively and clearly indicated that the local social incidents caused significant disruptions to inbound tourism and consumption-related sectors in the second half of 2019. The retail, restaurant, accommodation and inbound tourism sectors were particularly hard hit, with their business performances deteriorating sharply in the second half of 2019 at a pace² not seen for many years (*Chart 1*) which was apparently disproportionate to the external developments during the period. As such, the bulk of the enlarged declines in business in these sectors in the second half of the year conceivably reflected the significant disruptions by the local social incidents and violent acts. Therefore, by comparing the business performances of these sectors between the second quarter and the second half of the year, and making reference to the operating statistics of the affected sectors (including those on the relationship between their business receipts and value added) and the interrelations among different sectors obtained from the Census and Statistics

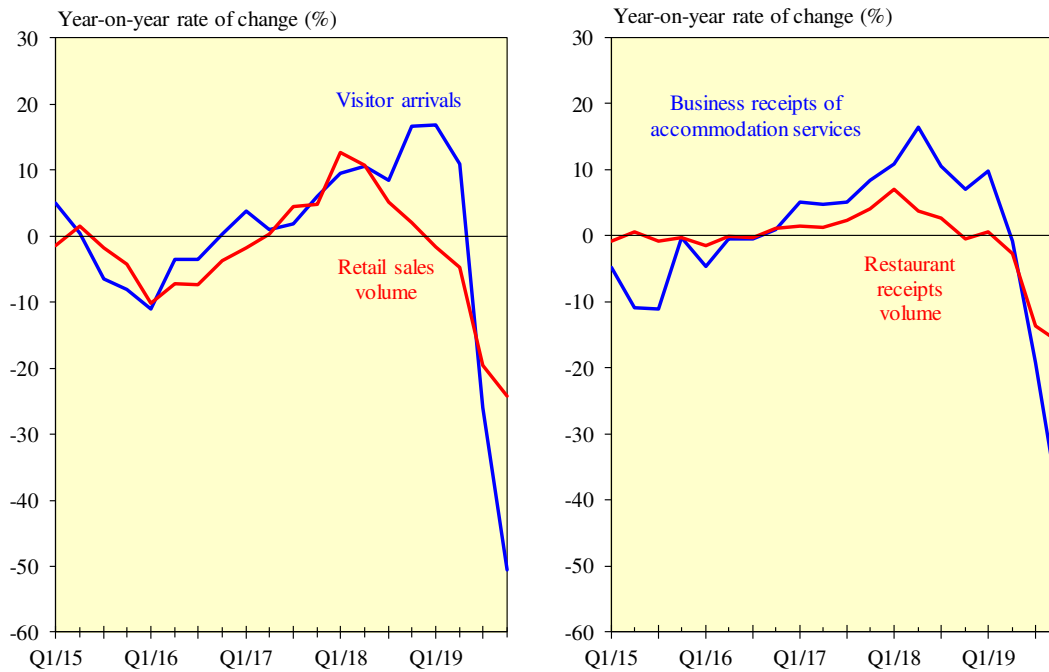
1 Economic Letter 2020/03 of the Office of the Government Economist entitled "Possible economic losses caused by the recent social incidents" (January 2020).

<https://www.hkeconomy.gov.hk/en/pdf/el/el-2020-03.pdf>

2 In the second half of 2019, the year-on-year decline in the volume of retail sales enlarged markedly to 21.9% from the 4.7% in the second quarter. The decline in restaurant receipts in real terms widened visibly to 14.9% in the second half of the year from the 2.7% in the second quarter. Visitor arrivals drastically turned to a 39.1% decline in the second half of the year from a 10.9% increase in the second quarter. As for hotel sector, the decline in business receipts of accommodation services accelerated noticeably to 31.5% in the second half of the year from 0.9% in the second quarter.

Department's (C&SD) annual survey, the economic losses caused by the local social incidents can be crudely estimated.

Chart 1 : The performances of the retail, restaurant and accommodation sectors and visitor arrivals saw abrupt deterioration in the second half of 2019



4. Economic losses are calculated in terms of value added in 2018 prices, which mainly includes profits and income. It is worth noting that a fall in business receipts in one sector does not only cause direct economic losses for that sector, but also leads to indirect economic losses for other supporting sectors.

III. ESTIMATION RESULTS

5. By comparing C&SD's data in the second quarter and the second half of 2019, it is estimated that the recent local social incidents resulted in **additional** declines in retail sales volume, restaurant receipts and business receipts for the accommodation sector, of around 17, 12 and 31 percentage points respectively in the second half of the year. Moreover, visitor arrivals turned abruptly to a year-on-year decline of 39.1% in the second half of 2019, from a 10.9% increase in the second quarter, which also led to a plunge in other tourists' consumption expenditure in Hong Kong in the second half of the year. In sum, the disruptions to the retail, restaurant and accommodation sectors as well as other tourists'

consumption expenditure due to the local social incidents are crudely estimated to bring about possible economic losses of **about \$40 billion** in total (in 2018 prices) in the second half of 2019, **equivalent to about 2.7% of GDP in the second half of 2018**³ (*Table 1*).

6. Hence, by taking account of the economic impacts on these tourism- and consumption-related sectors only, of the 2.9% year-on-year economic contraction in the second half of 2019, around 2.7 percentage points were attributable to the impacts of such factors as violent acts and social unrest. Apart from the direct economic losses for these sectors, the indirect economic losses for other supporting sectors are also taken into account.

7. Other factors could also have contributed to the worsening of the business in the retail, restaurant and accommodation sectors as well as other tourists' consumption expenditure in the second half of 2019. For instance, the escalation of US-Mainland trade tensions in the third quarter led to a drop in the local stock market and dampened consumption sentiment, which to some extent affected the retail and restaurant sectors. Yet, the local stock market recouped some lost ground in the fourth quarter as both sides resumed trade negotiations. Hence, external factors and the wealth effect⁴ arising from the asset market swings in the second half could hardly explain the abrupt deterioration of inbound tourism and consumption-related sectors during the period.

8. With a view to taking a comprehensive account of external factors, we have also utilised an internal econometric model to estimate how the Hong Kong economy would have performed in the second half of 2019 if the local social incidents did not ever occur. The estimate was then compared with the actual figures to gauge the economic losses due to the local social incidents.

3 According to the chain volume measures of GDP by economic activity, the decline in the value added of the retail sector in real terms enlarged markedly to 23.5% in the second half of 2019 from 4.7% in the second quarter. The decline in the value added of the restaurant sector in real terms widened visibly to 18.2% in the second half of the year from the 3.1% in the second quarter. The value added of the accommodation sector in real terms turned to a marked decline of 19.9% in the second half of the year from a 1.4% increase in the second quarter. If crudely estimated with reference to the worsening in value added in the second half of the year, the severe setbacks in these sectors and the decline in other tourists' consumption expenditure caused by the local social incidents would entail economic losses of about 2.8 percentage points of GDP in the second half of 2019, somewhat higher than the estimate in this article.

4 The Hang Seng Index edged down by 1.2% from end-June to end-December 2019, while residential property price index eased modestly by 3.7% between June and December. Past research by Hong Kong's scholars and analysts indicates that the wealth effect on consumption and the economy due to such magnitude of change would be rather limited. For more details, please refer to Economic Letter 2019/05 of the Office of the Government Economist entitled "Quantitative analysis of wealth effects on private consumption expenditure in Hong Kong" (May 2019).
<https://www.hkeconomy.gov.hk/en/pdf/el/el-2019-05.pdf>

9. As inbound tourism and local consumption were particularly hard hit by the social unrest in the second half of 2019, they should have understandably fared much better in the absence of the local social incidents. For inbound tourism, our internal econometric estimate suggested that visitor arrivals would have showed at least some modest growth in the second half if the local social environment had remained safe and stable, following a double-digit growth in the first half. Meanwhile, as discussed in *paragraph 7*, external developments alone were not likely to inflict a significant impact on the consumption-related sectors in the second half of 2019, though local consumption sentiment might still see some worsening amid the global economic slowdown and US-Mainland trade tensions. Based on these assumptions on visitor arrivals and local consumption sentiment, and also taking into account other developments, the estimate on economic losses derived from this econometric method is more than 3 percentage points of GDP, higher than the estimate as discussed in *paragraph 5-6*.

IV. CONCLUDING REMARKS AND CAVEATS

10. It is worth noting that, as the local social incidents involving violent acts dampened overall economic and investment sentiment, the consumption expenditure of local residents on sectors other than retail, restaurant and accommodation services as well as investment expenditure of business enterprises conceivably were also affected. The estimation as discussed in *paragraphs 3-6* has not fully taken such factors into account, and the results should thus be on the conservative side.

Table 1 : Crude estimates of the economic losses arising from the decline in businesses of the retail, restaurant and accommodation sectors, as well as that of other tourists' consumption expenditure in the second half of 2019

	Retail sector ^(*)	Restaurant sector ^(^)	Accommodation sector ^(@)	Other tourists' consumption expenditure ^(α)	Total
Additional losses in business receipts / visitor arrivals, comparing the second half of the year with the second quarter	Around 17 percentage points (Business receipts)	Around 12 percentage points (Business receipts)	Around 31 percentage points (Business receipts)	Around 50 percentage points (Visitor arrivals)	
	(\$ billion, 2018 prices)				
Direct economic losses	7.34	3.64	5.07	5.92	21.97
Indirect economic losses ^(#)	9.66	2.97	1.94	3.37	17.94
Direct and indirect economic losses ^(β)	17.00	6.61	7.01	9.29	39.91
Notes : (#)	The supporting industries for retail, restaurant and accommodation sectors as well as other tourists' consumption expenditure include the import/export trade, wholesale trade, transportation and finance sectors, among others.				
(*)	The value added of the retail sector amounted to \$88.3 billion in 2018, with a 3.3% direct contribution to GDP (at basic prices).				
(^)	The value added of the restaurant sector amounted to \$60.2 billion in 2018, with a 2.2% direct contribution to GDP (at basic prices).				
(@)	The value added of the accommodation sector amounted to \$31.3 billion in 2018, with a 1.2% direct contribution to GDP (at basic prices).				
(α)	The value added of other tourists' consumption expenditure amounted to \$32.2 billion in 2018, with a 1.2% direct contribution to GDP (at basic prices).				
(β)	Direct and indirect economic losses are crudely estimated by comparing the business performances of these sectors in the second quarter and the second half of 2019, and making reference to the operating statistics obtained from C&SD's annual survey.				