

**Business performance and operating situation of
low-paying sectors in 2018**

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Abstract

Based on the 2018 Annual Survey of Economic Activities conducted by the Census and Statistics Department, this letter article analyses the business performance and operating situation of low-paying sectors (in which relatively more low-paid employees are employed) and the small and medium-sized enterprises therein. The data show that the overall profitability of low-paying sectors remained weaker than in other sectors in 2018, and the overall profitability of small and medium-sized enterprises in the low-paying sectors was weaker than that of enterprises of all sizes in low-paying sectors. The overall profit ratio of small and medium-sized enterprises in some low-paying sectors (e.g. retail, and food and beverage services) was particularly low.

I. INTRODUCTION

1. Based on the 2018 Annual Survey of Economic Activities conducted by the Census and Statistics Department (C&SD)¹, this letter article analyses the business performance and operating situation of low-paying sectors (LPS) (in which relatively more low-paid employees were employed)² and the small and medium-sized enterprises³ (SMEs) therein⁴.

II. BUSINESS RECEIPTS

2. The overall business receipts of LPS rose by 7.7% in 2018, faster than its 4.1% increase in 2017 (**Chart 1**). Most sub-sectors within LPS continued to see growth in business receipts to varying extents. Thanks to the vibrant inbound tourism and solid local consumption back in 2018, the business receipts of the retail sector (which accounted for close to 70% of total business receipts in LPS) picked up notably in growth and those in the food and beverage services (F&B) sector (which accounted for close to 20% of the LPS total) accelerated somewhat, thereby leading to a visibly faster increase in business receipts in LPS. At the same time, the business receipts of the estate management, security and cleaning sector regained slight growth, while business receipts of other LPS continued to sustain increases. Business receipts of other sectors (i.e. non-LPS) rose by 5.8% in 2018, faster than their 4.3% increase in 2017.

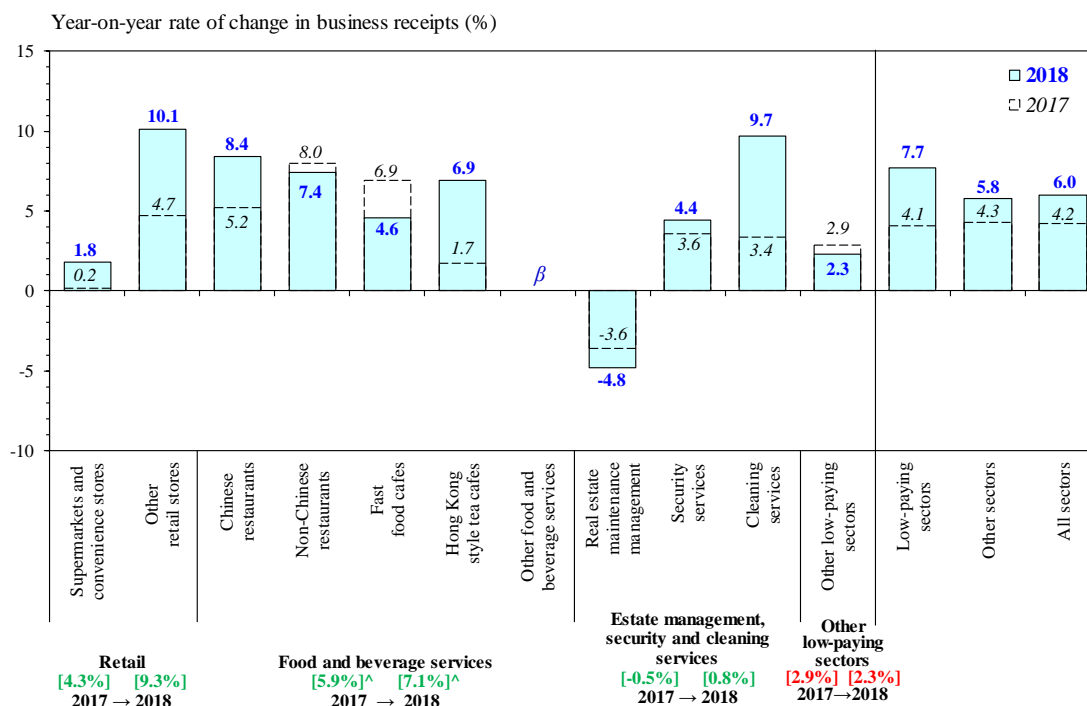
1 The statistics of the Annual Survey of Economic Activities cited in this article are in value terms and only pertain to enterprises with employees.

2 The Minimum Wage Commission (MWC) defined “low-paying sectors” (LPS) as sectors employing relatively more low-paid employees or sectors with a relatively higher proportion of low-paid employees. Based on the above criteria and the results of the 2018 Annual Earnings and Hours Survey, the current term of MWC (2019-2021), in reviewing the coverage of the LPS, decided to include the sub-sector of “other food service activities” (including beverage serving places and event catering among others) which had been under “other sectors” (i.e. non-LPS), as part of the “restaurants” sector under LPS, and name it as “other food and beverage services”. The “restaurants” sector was also renamed as “food and beverage services”. In this article, the 2017 figures and the year-on-year changes in 2018 are based on the definition of LPS before the revision, whereas the 2018 figures are compiled based on the latest definition.

3 SMEs are enterprises with fewer than 50 persons engaged.

4 For the business performance of enterprises in LPS in previous years, please see Box 6.1 in *2012 Economic Background and 2013 Prospects*, and the box articles in Chapter 5 of the First Quarter Economic Reports each year from 2014 to 2019.

Chart 1 : In 2018, business receipts in LPS picked up visibly in growth, driven by the retail and F&B sectors



Notes: (β) The year-on-year change is not available.

[] Figures in brackets denote the year-on-year rate of change in business receipts in that sector in the specified year.

([^]) Only includes Chinese restaurants, non-Chinese restaurants, fast food cafes and Hong Kong style tea cafes.

Source: Annual Survey of Economic Activities, C&SD.

III. OPERATING EXPENSES

3. In 2018, total operating expenses⁵ of enterprises generally increased alongside business expansion. Total operating expenses in LPS increased by 6.9%. The three major components of total operating expenses (compensation of employees; rent, rates and government rent; and other operating expenses⁶) in LPS increased by similar extents (by about 6% to 7%) in 2018. They contributed 3.0, 1.8 and 2.1 percentage points respectively to the increase in total operating expenses (**Chart 2**), or 44%, 26% and 30% of the increase respectively. These contributions were similar to their respective shares in total operating expenses⁷.

5 Cost of goods sold (i.e. cost incurred from materials or goods for re-sale) is excluded.

6 Other operating expenses include interest expenses, electricity, water, fuel, repair and maintenance, insurance costs, depreciation and amortisation charges, etc.

7 In 2018, compensation of employees accounted for around 40% of total operating expenses in LPS. Rent, rates and government rent accounted for another 30% and other operating expenses accounted for the remaining 30%.

4. Among LPS, apart from the sub-sector of real estate maintenance and management⁸, the total operating expenses of all other sub-sectors rose together with business expansion. The total operating expenses of some labour-intensive sectors such as F&B, security services and cleaning services were visibly more affected by the increase in compensation for employees⁹. The total operating expenses of the retail sector were more affected by the increases in rent and other operating expenses¹⁰. Furthermore, in many sub-sectors in LPS, other operating expenses also increased as business activities grew.

5. Out of the 5.9% increase in total operating expenses in other sectors, nearly 80% (4.8 percentage points) was attributable to the increase in other operating expenses. This was partly because other operating expenses accounted for close to 60%¹¹ of the total operating expenses for these sectors as a whole, and also partly because other operating expenses in these sectors rose markedly (by around 8%) in 2018, faster than those in compensation of employees and rent, rates and government rent (both rose by around 3%).

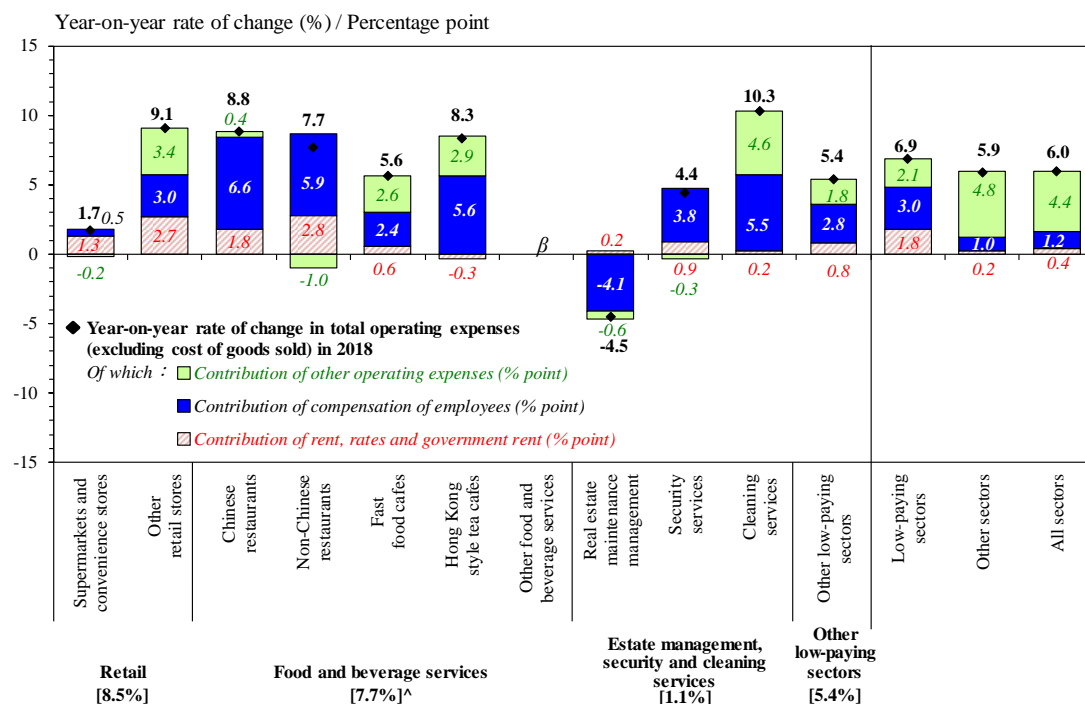
8 The total operating expenses of real estate maintenance and management fell by 4.5%, similar to its decline in business receipts (4.8%).

9 In 2018, compensation of employees accounted for around 40% to 80% of total operating expenses in security services, cleaning services and the various sub-sectors of F&B.

10 In 2018, rent, rates and government rent accounted for around 40% of total operating expenses in the retail sector. Compensation of employees and other operating expenses each accounted for around 30% of total operating expenses.

11 In 2018, compensation of employees accounted for around 35% of the total operating expenses in other sectors, whereas rent, rates and government rent accounted for around 5%, and other operating expenses accounted for around 60% of total operating expenses.

Chart 2 : In 2018, total operating expenses in the F&B sector were affected more visibly by rises in compensation of employees, whereas those in the retail sector were more affected by increases in rent and other operating expenses



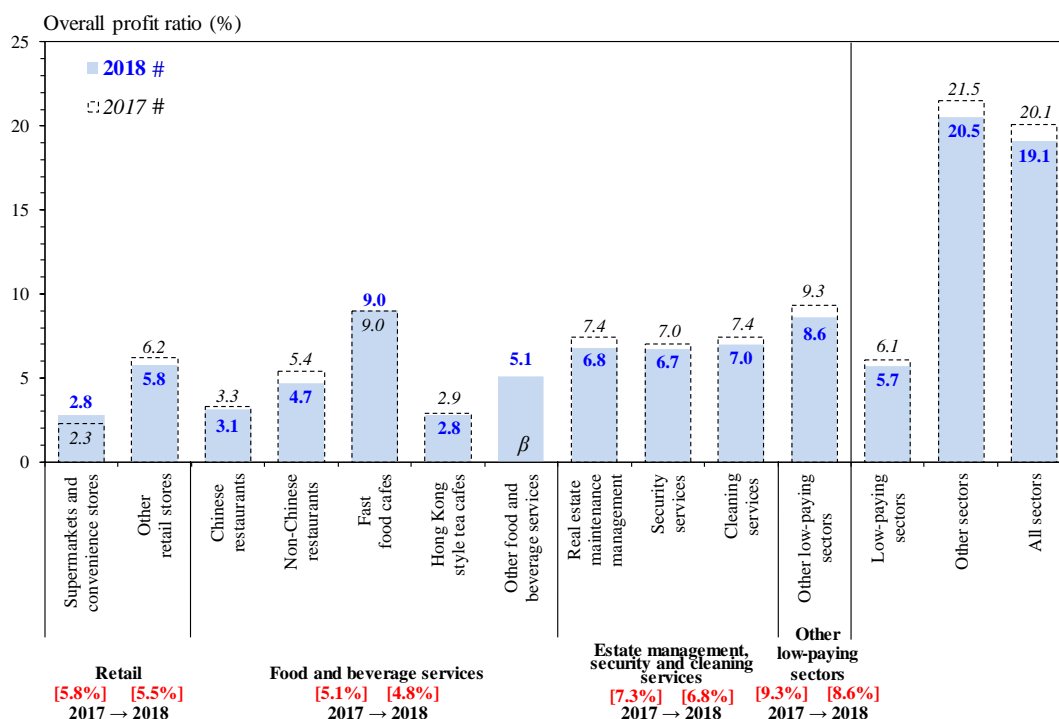
Notes: (β) The year-on-year change in 2018 is not available.
 [] Figures in brackets represent the year-on-year rate of change in total operating expenses (excluding cost of goods sold) of all enterprises in that sector in 2018.
 (^) Only includes Chinese restaurants, non-Chinese restaurants, fast food cafes and Hong Kong style tea cafes.

Source: Annual Survey of Economic Activities, C&SD.

IV. PROFITABILITY

6. The overall profit ratio of LPS was 5.7%, slightly lower than the ratio of 6.1% in 2017 (**Chart 3**). The profitabilities of most sub-sectors in LPS were slightly lower than in 2017, though for different reasons. The decline in profitability of the retail sector was mainly due to a faster rise in the cost of goods sold than of business receipts, while the profitability of the F&B sector was mainly dampened by a visible increase in compensation of employees. For other sectors (i.e. non-LPS), the overall profitability in 2018 was 20.5%, a decrease of 1.0 percentage point from 2017, mainly due to lower profitability in the finance, insurance, real estate, professional and business services sector. It is worth noting that the overall profit ratio of LPS remained noticeably lower than that of other sectors during the same period, indicating that the overall profitability of LPS continued to be weaker.

Chart 3 : In 2018, the overall profit ratio of LPS was slightly lower than in 2017, and remained noticeably lower than in other sectors



Notes: (#) The profit ratios in 2018 are based on the revised LPS coverage, whereas the 2017 figures are based on the LPS coverage before revision.

(β) The profit ratio in 2017 is not available.

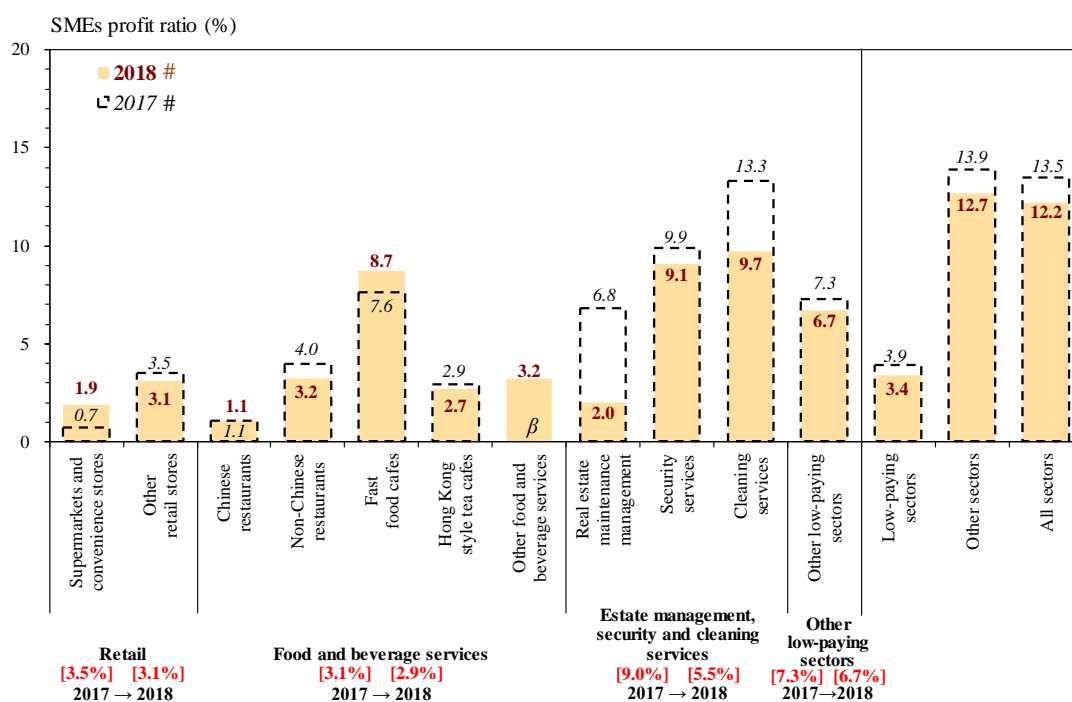
[] Figures in brackets represent the overall profit ratio of the sector in the specified year.

Source: Annual Survey of Economic Activities, C&SD.

V. BUSINESS PERFORMANCE AND OPERATING SITUATION OF SMEs

7. The business receipts of SMEs in LPS increased by 9.8% in 2018, faster than the overall increase in business receipts in LPS (7.7%) as a whole. At the same time, total operating expenses of SMEs in LPS rose by 12.2% in 2018, which was also faster than compared with LPS (6.9%) as a whole. The overall profit ratio of SMEs in LPS in 2018 was 3.4% in 2018, 0.5 percentage point lower than in 2017 (**Chart 4**). It was also visibly lower than the overall profit ratio of SMEs in other sectors (12.7%).

Chart 4 : In 2018, the overall profit ratio of SMEs in LPS was lower than in 2017



Notes: (#) The profit ratios in 2018 are based on the revised LPS coverage, whereas the 2017 figures are based on the LPS coverage before revision.

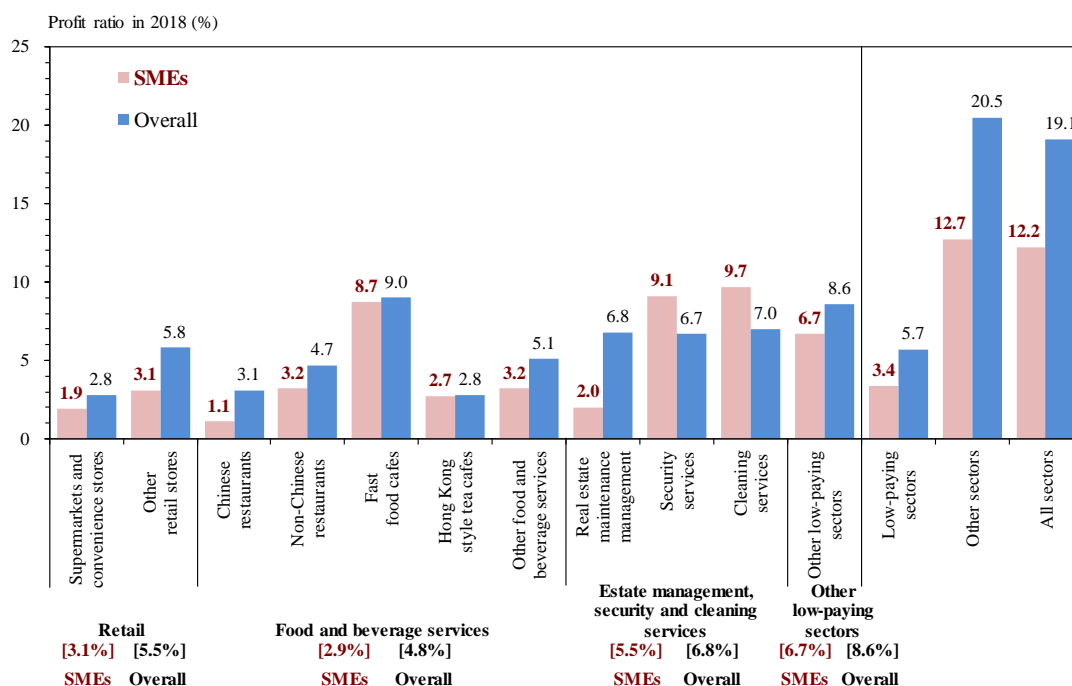
(β) The profit ratio in 2017 is not available.

[] Figures in brackets represent the profit ratio of SMEs of the sector in the specified year.

Source: Annual Survey of Economic Activities, C&SD.

8. Meanwhile, the overall profit ratio of SMEs in LPS in 2018 (3.4%) continued to be lower than the overall profit ratio of LPS as a whole (5.7%). This was also the case in many sub-sectors within LPS. For examples, overall profit ratios of SMEs in the retail and F&B sectors were 3.1% and 2.9% respectively in 2018, lower than the overall profit ratios of the corresponding sectors as a whole (5.5% and 4.8%, respectively) (**Chart 5**). Compared with large enterprises, SMEs are constrained by resources and may not be able to benefit from economies of scale and more effective management. They are also generally less capable of passing on and coping with increases in operating costs, and have less flexibility in deploying their resources. The profitability of SMEs in LPS is hence generally weaker than that of larger enterprises.

Chart 5 : The overall profitability of SMEs remained weaker, with the overall profit ratios of SMEs in the retail and F&B sectors particularly low



Note: [] Figures in brackets denote the profit ratio of all enterprises and SMEs in that sector in 2018.
Source: Annual Survey of Economic Activities, C&SD.

9. Among SMEs in LPS, the overall profit ratios of the retail and F&B sectors were particularly low. Among them, SMEs of certain sub-sectors such as Chinese restaurants and supermarkets and convenience stores only earned meagre profits, with their profit ratios being just 1.1% and 1.9% respectively.

VI. CONCLUDING REMARKS

10. The 2018 data show that the overall profitability of LPS remained weaker than in other sectors, and the overall profitability of SMEs in LPS was even weaker than in the LPS as a whole. The overall profitability of SMEs in some LPS (such as retail and F&B) was particularly low. Against this background, these LPS with lower profitability would face greater pressure when facing negative shocks, and there is a higher chance that they would need to cut costs by slashing manpower or wages.

11. This situation is reflected in the employment figures in recent months. According to the Quarterly Survey of Employment and Vacancies conducted by C&SD, the number of persons engaged in the private sector fell by 3.8% year-on-year in March 2020, the largest year-on-year decrease since December 1998 when the economy was hard hit by the Asian financial crisis. For sectors within LPS, the number of persons engaged in the retail and F&B sectors plummeted by 6.5% and 12.0% respectively in

March 2020. More recent statistics compiled from the General Household Survey conducted by C&SD, though not strictly comparable to those from the business establishment surveys, showed that total employment plunged further by 6.5% year-on-year in the second quarter of 2020, the largest decline on record. The declines in employment in the retail and F&B sectors were also more pronounced. These data not only reflect that these two LPS are more affected by the COVID-19 epidemic and the social distancing measures thus implemented, but also that the enterprises in these sectors, after having experienced the recession in the second half of 2019, only had limited room to deal with the abrupt worsening of the business environment and had to resort to cutting manpower to reduce operating expenses.