

CHAPTER 1 : OVERVIEW OF ECONOMIC PERFORMANCE

Summary

- *Following the full-fledged upturn in 2017, the Hong Kong economy stayed vibrant in the first quarter of 2018, turning in a robust growth of 4.7% over a year earlier. External demand picked up as the global economy sustained broad-based momentum. Domestic demand also strengthened, buttressed by favourable labour market conditions and positive business sentiment.*
- *Total exports of goods grew strongly in the first quarter as the upswing in global investment and trade translated into booming production and trading activities in Asia. Exports of services also picked up visibly, with an extra boost from a strong recovery in inbound tourism and active global financial market activities. Lately, increased trade tensions between the US and the Mainland have clouded the external trade outlook. The developments down the road are still uncertain and need to be monitored closely.*
- *Domestic demand continued to strengthen in the first quarter. Private consumption expenditure grew notably, reflecting generally optimistic consumer sentiment on the back of stronger income and asset market conditions. Overall investment expenditure registered further growth, amid notable growth in machinery and equipment acquisition as well as modest expansion in building and construction activity.*
- *The labour market was tight. The seasonally adjusted unemployment rate stayed at a 20-year low of 2.9% in the first quarter, while the underemployment rate showed a further decline. Total employment continued to record sturdy growth. In tandem, wages and earnings continued to register real improvements.*
- *The local stock market was bullish on entering 2018, but experienced corrections in the latter part of the first quarter amid a firmer outlook for gradual US interest rate hikes and intensified concerns over the global trading environment. Separately, the residential property market remained buoyant, with flat prices rising further amid active trading.*
- *Consumer price inflation was moderate in the first quarter, though going up somewhat due partly to favourable global and local economic situations and partly to some temporary factors. Local cost pressures stayed largely in check. External price pressures also remained moderate, though import prices picked up slightly given the weakness in the US dollar over the past year and the mild acceleration in inflation in some of our major import sources.*

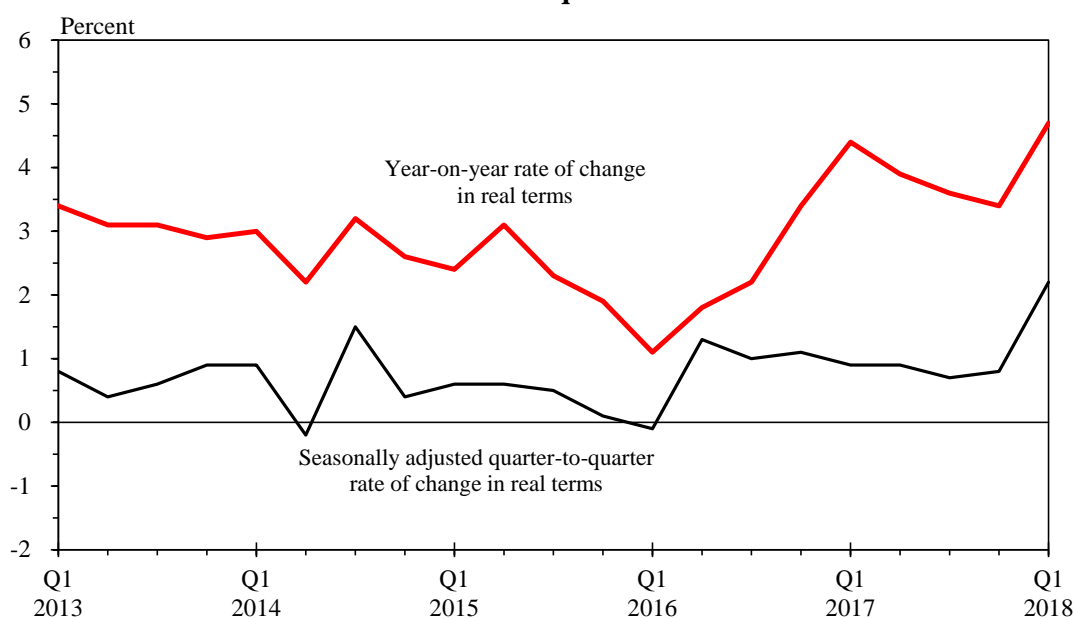
Overall situation

1.1 The Hong Kong economy stayed vibrant, expanding notably by 4.7% in the first quarter of 2018 over a year earlier and strengthening from its 3.8% growth rate in 2017. With the global economy maintaining its broad-based momentum, there was strong external demand for Hong Kong's exports, which grew robustly in the first quarter. The continued expansion of trade flows, together with the strong recovery of inbound tourism and active global financial market activities, also saw exports of services register faster growth. Domestically, private consumption expenditure continued to display strength as consumer sentiment was well anchored by favourable labour market conditions. Overall investment expenditure grew moderately, supported by notable increases in machinery and equipment acquisition, active property transactions, and modest expansion in building and construction activity. Meanwhile, business sentiment stayed generally positive. The labour market remained tight, with strong employment growth and solid increases in wages and earnings. Consumer price inflation was moderate, though going up somewhat from the preceding quarter due to strengthening economic conditions as well as certain temporary factors.

1.2 While the expansion of the global economy has become more established, as reflected in the latest forecasts by the International Monetary Fund (IMF) in mid-April⁽¹⁾, there are still uncertainties prevailing in the external environment. In the first quarter, all major economies continued to perform well. The strength in the US economy, fanned by fiscal expansion by the US government in the form of tax cuts, not only prompted the Federal Reserve to raise the Federal Funds Rate again in March, but also firmed up market expectations of further US interest rate hikes going forward. The shift in market expectations on the pace of US interest rate normalisation increased the volatility in financial markets worldwide. The local stock market also experienced corrections in the latter part of the first quarter. More recently, trade tensions between the US and the Mainland have increased and become a key source of uncertainty surrounding the external trading environment.

1.3 In the first quarter of 2018, *Gross Domestic Product* (GDP)⁽²⁾ grew notably by 4.7% in real terms over a year earlier, up from 3.4% growth in the preceding quarter (same as the earlier estimate), marking the sixth consecutive quarter of growth above the trend growth rate of 2.7% per annum in the past ten years. On a seasonally adjusted quarter-to-quarter comparison⁽³⁾, real GDP surged by 2.2% in the first quarter, up from 0.8% in the preceding quarter (same as the earlier estimate).

Diagram 1.1 : The Hong Kong economy stayed vibrant and expanded robustly in the first quarter



The external sector

1.4 *Total exports of goods* compiled under the GDP accounting framework picked up to show a notable year-on-year growth of 5.2% in real terms in the first quarter, from that of 3.4% in the preceding quarter. Analysed by major market, with reference to external merchandise trade statistics, exports to Asian markets as a whole continued to show robust growth on the back of buoyant manufacturing activities in the region that created solid demand for exports of raw materials and semi-manufactures. In particular, exports to the Mainland saw a visible pick-up in growth. Also, exports to the US and the EU increased sizably, thanks to sustained improvement in final demand in these economies.

1.5 *Exports of services* likewise displayed strength in the first quarter, with broad-based growth of 7.5% in real terms over a year earlier, up from 3.9% growth in the preceding quarter and 3.2% growth for 2017 as a whole. Exports of travel services strengthened to show double-digit growth, reflecting the strong recovery of inbound tourism. Notwithstanding the somewhat more volatile financial markets in the first quarter, the solid momentum in the global economy underpinned active financial market activities, resulting in sizable growth in exports of financial services. Exports of transport services expanded solidly amid vibrant regional trade flows, while exports of business and other services grew modestly.

**Table 1.1 : Gross Domestic Product, its main expenditure components
and the main price indicators
(year-on-year rate of change (%))**

	<u>2016</u> [#]	<u>2017</u> [#]	<u>2017</u>				<u>2018</u>
			<u>Q1</u> [#]	<u>Q2</u> [#]	<u>Q3</u> [#]	<u>Q4</u> [#]	<u>Q1</u> ⁺
<i>Change in real terms of GDP and its main expenditure components (%)</i>							
Private consumption expenditure	2.0	5.5	3.7 (0.8)	5.8 (2.0)	6.3 (1.8)	6.3 (1.5)	8.6 (3.1)
Government consumption expenditure	3.3	3.4	2.8 (0.6)	3.0 (1.1)	4.5 (1.7)	3.2 (-0.2)	3.9 (1.2)
Gross domestic fixed capital formation	-0.1	3.5	5.7	7.6	-2.1	3.1	3.8
Building and construction	5.9	1.7	7.0	2.0	0.9	-2.6	1.0
Costs of ownership transfer	-2.9	22.3	77.8	53.0	-12.8	6.2	12.8
Machinery, equipment and intellectual property products	-6.3	1.8	-7.8	6.1	-3.0	9.9	6.2
Total exports of goods ^{&}	1.6	5.9	9.6 (1.2)	5.7 (0.1)	5.7 (0.8)	3.4 (1.1)	5.2 (3.1)
Imports of goods ^{&}	0.7	7.0	10.3 (0.8)	6.4 (0.4)	6.3 (1.5)	5.4 (2.4)	6.9 (2.3)
Exports of services ^{&}	-3.5	3.2	3.3 (1.2)	1.9 (-1.6)	3.5 (3.0)	3.9 (1.2)	7.5 (4.8)
Imports of services ^{&}	2.0	1.9	0.9 (0.2)	4.8 (1.6)	1.4 (-1.7)	0.8 (0.8)	3.8 (3.2)
Gross Domestic Product	2.2	3.8	4.4 (0.9)	3.9 (0.9)	3.6 (0.7)	3.4 (0.8)	4.7 (2.2)
<i>Change in the main price indicators (%)</i>							
GDP deflator	1.7	2.9	2.4 (0.9)	3.4 (1.1)	3.2 (0.3)	2.8 (0.5)	4.1 (2.1)
Composite CPI							
Headline	2.4	1.5	0.5 (0.1)	2.0 (0.6)	1.8 (0.3)	1.6 (0.6)	2.4 (0.9)
Underlying[^]	2.3	1.7	1.4 (0.1)	2.0 (0.6)	1.7 (0.3)	1.6 (0.6)	2.4 (0.8)
Change in nominal GDP (%)	3.9	6.8	6.8	7.4	6.9	6.3	9.1

Notes : Figures are subject to revision later on as more data become available. The seasonally adjusted quarter-to-quarter rate of change is not applicable to gross domestic fixed capital formation, as no clear seasonal pattern is found for the category due to the presence of considerable short term fluctuations.

(&) Figures are compiled based on the change of ownership principle in recording goods sent abroad for processing and merchanting under the standards stipulated in the *System of National Accounts 2008*.

(#) Revised figures.

(+) Preliminary figures.

() Seasonally adjusted quarter-to-quarter rate of change.

(^) After netting out the effects of the Government's one-off relief measures.

The domestic sector

1.6 The domestic sector continued to strengthen in the first quarter. *Private consumption expenditure* grew markedly by 8.6% in real terms in the first quarter over a year earlier. Local consumption sentiment was firmly supported by favourable job and income conditions as well as wealth effect from stronger asset market conditions. *Government consumption expenditure* continued to grow steadily by 3.9% in the first quarter, following its 3.2% growth in the preceding quarter.

**Table 1.2 : Consumer spending by major component^(a)
(year-on-year rate of change in real terms (%))**

	Total consumer spending in the domestic market ^(a)	<i>Of which :</i>						Private consumption expenditure ^(b)
		Food	Durables	Non- durables	Services	Residents' expenditure abroad	Visitor spending	
2017 Annual	5.1	3.6	6.0	6.4	4.8	4.0	1.5	5.5
H1	4.0	3.4	-0.9	5.6	4.2	5.2	*	4.8
H2	6.1	3.9	11.9	7.2	5.3	3.0	2.9	6.3
Q1	3.7	3.4	-1.1	5.2	4.1	-0.8	1.5	3.7
Q2	4.3	3.4	-0.6	5.9	4.3	11.5	-1.7	5.8
Q3	5.9	4.5	9.4	7.6	4.9	3.8	1.8	6.3
Q4	6.3	3.4	13.9	6.9	5.6	2.1	4.0	6.3
2018 Q1	9.3	4.1	25.7	13.9	6.0	6.1	11.6	8.6

Notes : (a) Consumer spending in the domestic market comprises both local consumer and visitor spending.

(b) Private consumption expenditure is obtained by deducting visitor spending from total consumer spending in the domestic market, and adding back residents' expenditure abroad.

(*) Change within $\pm 0.05\%$.

Diagram 1.2 : Private consumption expenditure accelerated to show notable growth

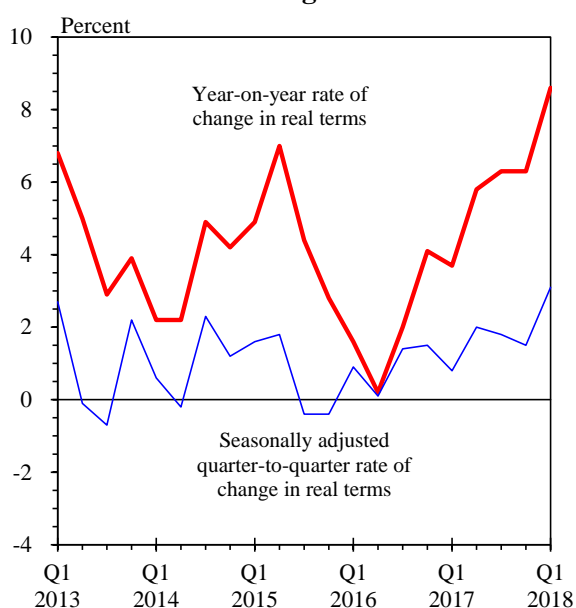
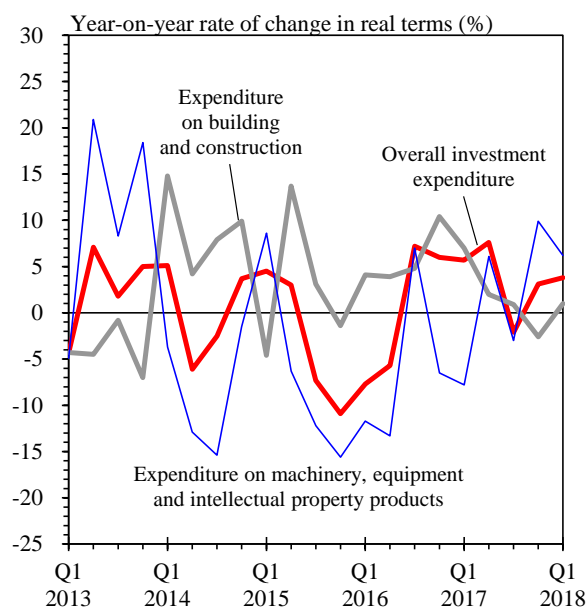


Diagram 1.3 : Overall investment spending continued to grow



1.7 Overall investment spending in terms of *gross domestic fixed capital formation* increased further by 3.8% year-on-year in real terms in the first quarter, following growth of 3.5% in 2017. Thanks to the sustained upturn in the global economy, local business sentiment was broadly positive in early 2018 (see **Box 1.1** for an analysis of business sentiments). This, together with the sizable increase in the machinery and equipment acquisition by the public sector, rendered a notable year-on-year increase in overall machinery and equipment acquisition. Overall building and construction activity saw modest growth in the first quarter on the back of expansion in public building and construction works. Costs of ownership transfer showed a double-digit increase as property market transactions went up visibly over a year earlier.

Box 1.1

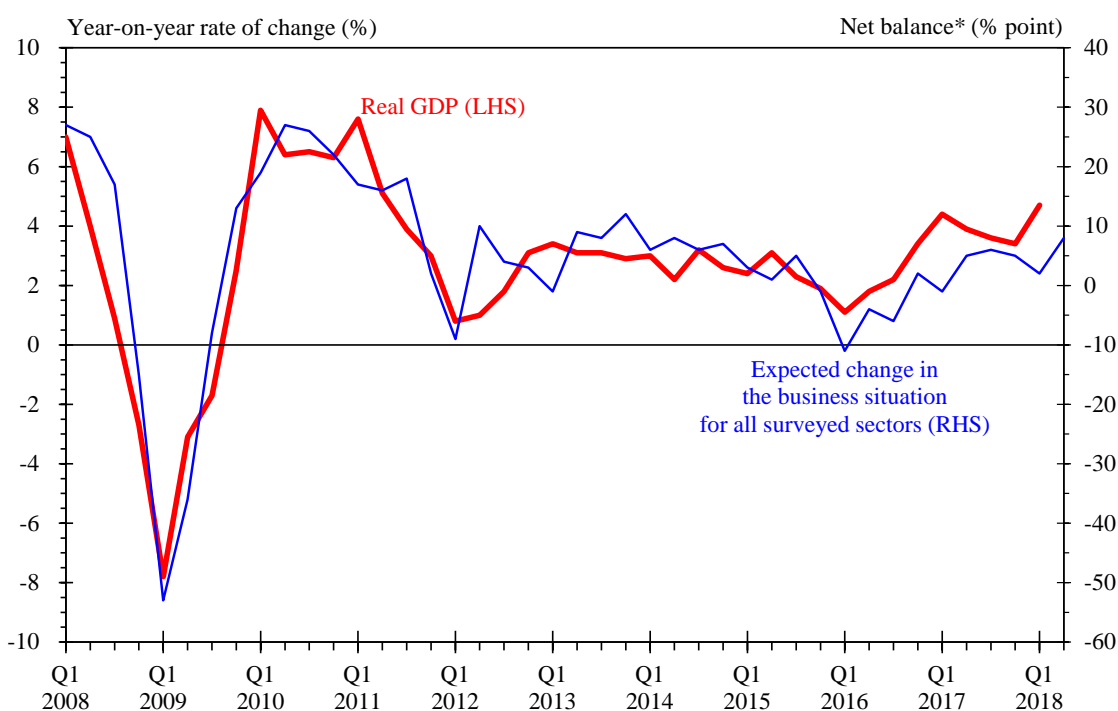
Business sentiment in Hong Kong

This box article gives a general overview of the prevailing business sentiment in Hong Kong, based on results from various surveys that are available in the public domain.

According to the latest results from the Census and Statistics Department (C&SD)'s Quarterly Business Tendency Survey (QBTS)⁽¹⁾, overall business sentiment of large enterprises in Hong Kong turned more upbeat of late, amid the benign global economic environment and sustained above-trend growth of the local economy (*Chart 1*). In particular, the proportion of large enterprises expecting a better business situation in the second quarter of 2018 outweighed that of those expecting a weaker one by 8 percentage points (i.e. a net balance of +8), the highest net balance since the second quarter of 2014. It should however be noted that the survey was conducted in early March to mid-April 2018, and so the respondents' expectations may not have fully taken into account the evolving situation surrounding the escalation of trade tensions between the US and the Mainland of late.

Among various sectors, large enterprises in "financing and insurance", "information and communications" and "real estate" were particularly optimistic (*Table 1*), thanks to robust economic conditions and buoyant property market. Business sentiment was broadly positive among large enterprises in "import/export trade and wholesale" and "retail" amid notable growth in external trade and consumption, while that in "manufacturing" and "construction" also saw relative improvement. On the other hand, large enterprises in "accommodation and food services", "transportation, storage and courier services" and "professional and business services" were more cautious. Meanwhile, hiring sentiment of large enterprises in most sectors was positive (*Table 2*), in line with prevailing sturdy employment growth.

Chart 1 : Large enterprises in Hong Kong turned more upbeat on their near-term business prospects



Note : (*) Net balance indicates the direction of expected change in the business situation versus the preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "better" over that choosing "worse". A positive sign indicates a likely upward trend while a negative sign, a likely downward trend.

(1) The Quarterly Business Tendency Survey collected views from around 500-600 large establishments on their near-term business outlook. Respondents were asked to exclude seasonal influences in their responses.

Box 1.1 (Cont'd)

Table 1 : Business sentiment for large enterprises in many sectors showed relative improvement

QBTS: Expected changes in business situation						
	Net balance* (% point)					
	2017				2018	
	Q1	Q2	Q3	Q4	Q1	Q2
Manufacturing	+18	+14	+18	-1	-10	-5
Construction	-18	-14	-9	-16	-16	-13
Import/export trade and wholesale	-6	-2	0	+1	-4	+5
Retail	-15	-4	-4	+24	+20	+4
Accommodation and food services	-14	-13	-2	+13	-3	-7
Transportation, storage and courier services	+7	-2	+2	-7	-5	-8
Information and communications	0	+19	+17	+16	-2	+20
Financing and insurance	+12	+24	+19	+13	+21	+28
Real estate	-2	0	+6	+6	0	+11
Professional and business services	-8	0	0	+7	+2	-2

Note: (*) Net balance indicates the direction of expected change in the business situation versus the preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "better" over that choosing "worse". A positive sign indicates a likely upward trend while a negative sign, a likely downward trend.

Table 2 : Hiring sentiment among large enterprises remained favourable

QBTS: Expected changes in number of persons engaged						
	Net balance* (% point)					
	2017				2018	
	Q1	Q2	Q3	Q4	Q1	Q2
Manufacturing	+10	-7	+21	+13	-10	+15
Construction	-8	0	+2	-9	-7	-8
Import/export trade and wholesale	0	+2	-1	+1	-2	+2
Retail	+1	+4	-3	+3	-1	+7
Accommodation and food services	+5	+9	+20	+5	+5	+7
Transportation, storage and courier services	+17	+9	+7	+2	+9	+8
Information and communications	+14	+24	+9	+10	-8	+9
Financing and insurance	+15	+16	+16	+13	+24	+26
Real estate	+28	+18	+14	+18	+5	+5
Professional and business services	0	+6	-3	+5	+4	+2

Note: (*) Net balance indicates the direction of expected change in the number of persons engaged versus the preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "up" over that choosing "down". A positive sign indicates a likely upward trend while a negative sign, a likely downward trend.

As for small and medium-sized enterprises (SMEs), the C&SD also compiled a set of diffusion indices on a monthly basis⁽²⁾ to gauge the general directions of change in the views of SMEs on their business situation versus the preceding month. The overall index on business receipts so far in 2018, while still below the 50.0 mark, held largely stable (*Chart 2a*). The feedbacks from SMEs consulted also continued to suggest a broadly stable employment situation and highly accommodative credit situation in recent months. Meanwhile, the Standard Chartered Hong Kong SME Leading Business Index (Standard Chartered SME Index)⁽³⁾ rose further in the second quarter of 2018, suggesting sustained relative improvement in SMEs' business outlook.

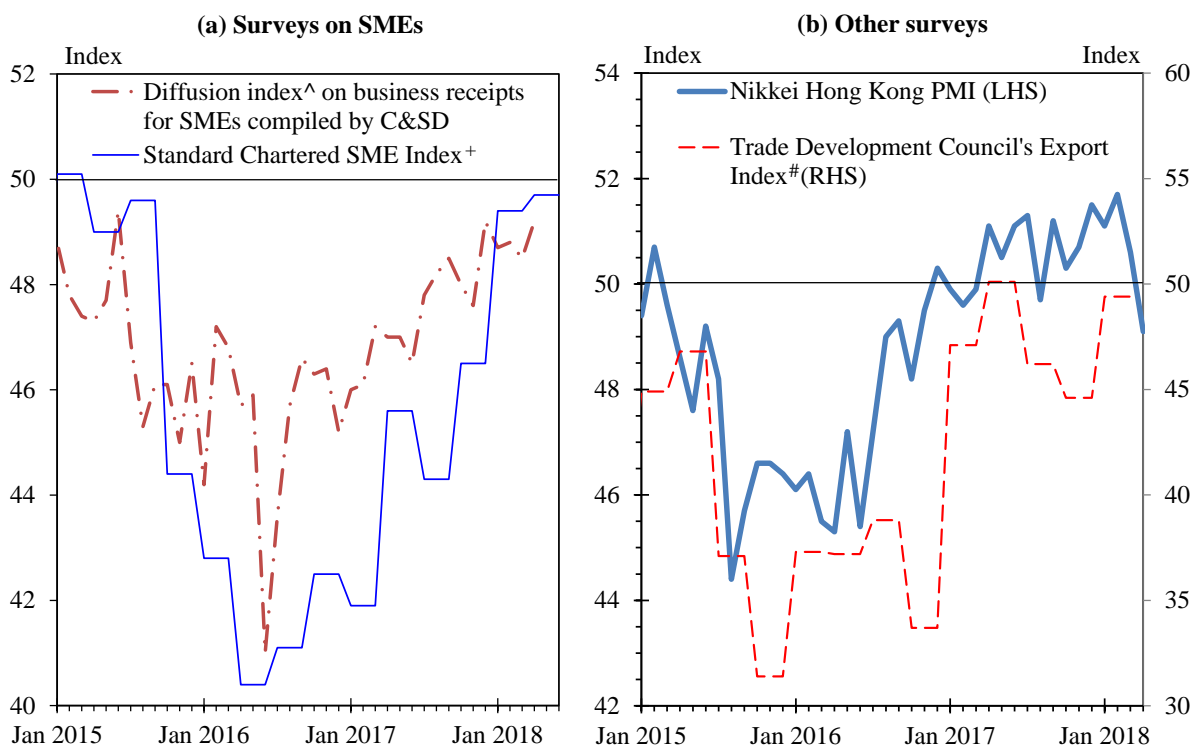
As for other surveys in the public domain, the Hong Kong Trade Development Council (HKTDC)'s Export Index⁽⁴⁾ rebounded to 49.4 in the first quarter of 2018, reflecting a more optimistic view of traders on the near-term export performance (*Chart 2b*). The report added that the majority of traders did not expect significant damage to Hong Kong's export performance due to the evolving situation in the trade relations between the US and the Mainland as the proposed measures had yet to materialise. But since the survey result was released in mid-March, it had yet to reflect the recent escalation of trade tensions between the US and the Mainland in April. For more recent indication, the monthly Nikkei Purchasing Managers' Index (PMI) of Hong Kong⁽⁵⁾, which gauges the performance of the private sector's business activity, dipped to 49.1 in April, after staying in the expansionary zone in the first three months of 2018. This pointed to more cautious business sentiment of late amid rising uncertainty over the external trading environment.

(2) It refers to the results from the Monthly Survey on the Business Situation of SMEs that solicits feedbacks from a panel sample of around 600 SMEs each month.

(3) Conducted independently by Hong Kong Productivity Council, the quarterly survey enables the public and SMEs to gain insights into the forthcoming business climate for better forward planning. The Overall Index comprises five areas, including local SMEs' outlook on their "Sales amount", "Profit margin", "Investments", "Staff number", and "Global economic growth" for the next quarter.

Box 1.1 (Cont'd)

Chart 2 : Other survey indicators pointed to improving business sentiment in the first quarter, though turning somewhat more cautious of late



Notes: (^) The diffusion index is computed by adding the percentage of SMEs reporting “up” to one half of the percentage of SMEs reporting “same”. A diffusion index reading above 50 indicates that the business condition is generally favourable, whereas an index below 50 indicates otherwise. Respondents were requested to exclude seasonal effects in reporting their views.

(+) Launched in Q3 2012 and quarterly data.

(#) A reading above 50 indicates that more than half of the surveyed traders incline towards the upside, which can be interpreted as an upward trend and an increase in confidence, and vice versa for a reading below 50.

It is worth pointing out that these surveys are essentially opinion-based, thereby unavoidably subject to various limitations (e.g. results are not directly comparable) and hence the results should be interpreted with care. Still, the latest survey findings taken together suggest that business sentiment in Hong Kong has remained largely positive thanks to the sustained global economic upswing, though turning somewhat more cautious of late amid rising uncertainties in the external environment, notably those stemming from the escalation in trade tensions between the US and the Mainland, as well as the ongoing monetary policy normalisation by the US. The Government will continue to closely monitor the global economic developments for their possible repercussions on the Hong Kong economy.

(4) The HKTDC Export Index is compiled based on a quarterly survey to collect views from around 500 traders concerning their export performances in the prevailing quarter as well as their outlook for the subsequent quarter and covers six major industries – electronics, clothing, jewellery, timepieces, toys and machinery.

(5) According to the press release jointly released by Nikkei and IHS Markit, the Nikkei Hong Kong PMI is compiled according to monthly replies to questionnaires sent to purchasing executives in over 300 companies. It is a composite index based on five individual indices with the following weights: New Orders (0.3); Output (0.25); Employment (0.2); Suppliers' Delivery Times (0.15); and Stock of Items Purchased (0.1), with the Delivery Times index inverted so that it moves in a comparable direction. Survey responses reflect the change, if any, in the prevailing month compared to the previous month.

The labour sector

1.8 The labour market remained tight, with the *seasonally adjusted unemployment rate* staying at a 20-year low of 2.9% in the first quarter of 2018. The *underemployment rate* edged down to 1.0%, also the lowest level in over 20 years. Total employment continued to grow sturdily over a year earlier. In tandem, wages and earnings registered further year-on-year improvements in real terms, with more notable increases in the lower-skilled segments of the labour market.

The asset markets

1.9 The *local stock market* turned more volatile in the first quarter of 2018 alongside other major stock markets worldwide. The Hang Seng Index continued its uptrend in January and reached a record high of 33 154 on 26 January 2018. Yet, as US economic growth gathered steam with solid job gains, a multi-year low unemployment rate and signs of uptick in inflationary pressure, market expectations on the near-term outlook of gradual US rate hikes firmed up during the quarter, adding volatility to global financial markets. Intensified concerns over trade tensions between the US and the Mainland also caused some jitters in the financial markets. The local stock market hence experienced some downward adjustments in the latter part of the first quarter, with the Hang Seng Index closing the quarter at 30 093, up by only 0.6% from end-2017 and down by 9.2% from its peak in late January. Nevertheless, average daily turnover of the stock market rose visibly to \$146.1 billion in the first quarter, from \$107.3 billion in the preceding quarter. Credit growth, in terms of the year-on-year increase in loans for use in Hong Kong (including trade finance), remained strong at 15.1% at end-March 2018, compared to 15.5% growth recorded three months earlier, as the demand for loans was strong amid a vibrant economy.

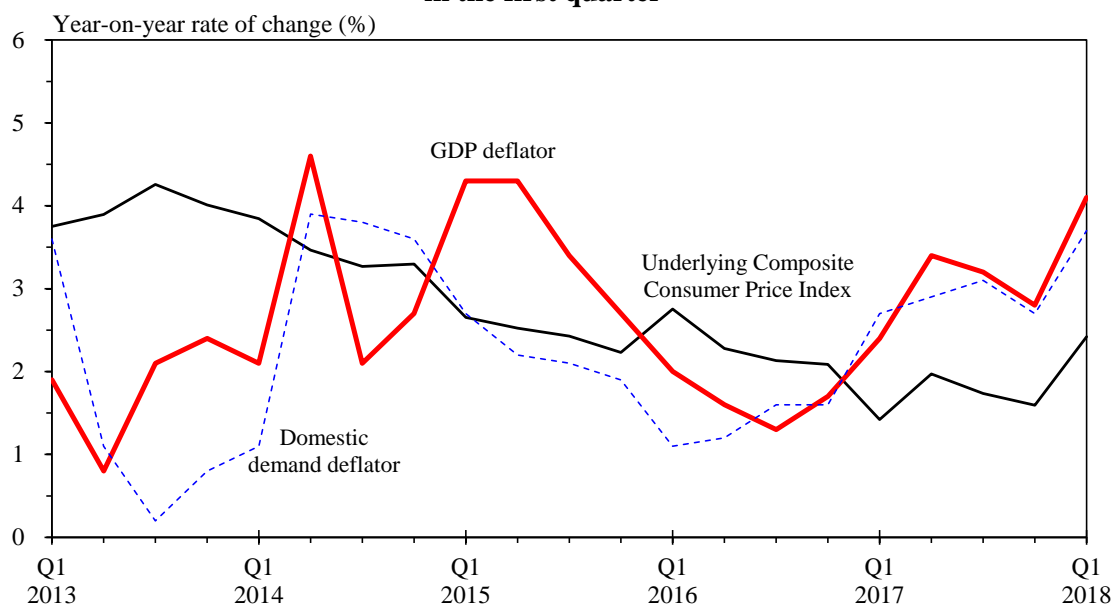
1.10 The *residential property market* remained buoyant in the first quarter of 2018. While trading volume was 8% lower than the fervent level in the preceding quarter, it was 14% higher than a year ago. Residential property prices increased by 4% between December 2017 and March 2018. Overall flat prices in March 2018 exceeded the 1997 peak by 113%, and the housing affordability ratio worsened to around 71% in the first quarter. Flat rentals rose by 1% during the first quarter. In contrast, office rentals stayed virtually flat over the same period, while those for retail premises fell by 1%.

Inflation

1.11 Consumer price inflation was moderate in the first quarter, though going up somewhat on the back of strong economic conditions as well as some temporary factors. Locally, labour cost pressure was held in check on a unit cost basis, as rises in wages and earnings were largely matched with concurrent growth in labour productivity. Commercial rental cost pressure was contained in general, while the increase in fresh-letting residential rentals over the past year or so continued to feed through gradually to consumer price inflation. External price pressures also remained moderate, only edging up slightly due to the weaker US dollar and mildly higher inflation in some major import sources amid the global economic upturn. Overall, netting out the effects of the Government's one-off relief measures, *underlying consumer price inflation* was 2.4% in the first quarter, up from 1.6% in the prior quarter. *Headline consumer price inflation* rose to 2.4% in the first quarter from 1.6% in the preceding quarter.

1.12 The year-on-year rate of increase in the *GDP deflator* climbed up to 4.1% in the first quarter from 2.8% in the prior quarter. The year-on-year increase in the domestic demand deflator likewise rose to 3.7%, partly driven by the modest rise in consumer price inflation. Meanwhile, the terms of trade saw a mild improvement, as export prices rose slightly faster than import prices.

Diagram 1.4 : Underlying consumer price inflation pressure went up somewhat in the first quarter



Note : The year-on-year rates of change of the Composite Consumer Price Index from the fourth quarter of 2015 onwards are computed from the new 2014/15-based series, and those before are from the old 2009/10-based series.

GDP by major economic sector

1.13 The growth in the net output of the services sector as a whole picked up to 3.5% in real terms in 2017 from 2.3% in 2016, as the local economy exhibited notable expansion amid a synchronised global economic upswing. The improvement was widespread across different segments. Specifically, alongside vibrant regional trading activities, the net output of import and export trade as well as that of transportation and storage grew solidly throughout 2017. Thanks to the revival in inbound tourism and positive local consumer sentiment, the net output of wholesale and retail trades recovered progressively over the course of 2017 and reverted to moderate growth for the year as a whole, while the net output of accommodation and food services also grew at a faster pace in 2017. The net output of the financing and insurance sector saw a pick-up in growth in 2017 amid more buoyant financial markets. The net output of public administration, social and personal services expanded steadily. The net output of real estate, which covers activities of private sector developers and property agencies, also saw further growth in 2017. Meanwhile, the net output of professional and business services saw further modest growth. As for the secondary sector, the net output of the construction sector continued to grow for 2017 as a whole, notwithstanding a decline in the final quarter against a higher base of comparison in the same quarter last year. Meanwhile, the net output of the manufacturing sector reverted to mild growth for the year as a whole.

**Table 1.3 : GDP by economic activity^(a)
(year-on-year rate of change in real terms (%))**

	<u>2016</u>	<u>2017</u>	<u>2016</u>				<u>2017</u>			
			<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>
Manufacturing	-0.4	0.4	-0.3	-0.4	-0.1	-1.0	0.2	0.4	0.3	0.8
Construction	5.1	2.3	1.8	3.0	4.6	10.7	7.3	3.2	2.0	-2.6
Services ^(b)	2.3	3.5	1.5	2.6	2.2	2.7	3.7	3.3	3.6	3.4
Import/export, wholesale and retail trades	0.6	3.6	-2.1	0.8	0.9	2.2	3.9	3.2	3.8	3.6
Import and export trade	2.2	3.9	-0.1	2.7	2.4	3.5	5.1	3.8	3.7	3.3
Wholesale and retail trades	-5.9	2.3	-9.7	-5.9	-5.9	-2.7	-0.8	0.6	4.0	4.6
Accommodation ^(c) and food services	0.5	2.3	-1.0	1.5	0.7	0.9	1.5	1.4	2.2	3.9
Transportation, storage, postal and courier services	3.0	4.9	2.3	3.0	3.1	3.5	4.7	4.9	5.0	4.9
Transportation and storage	3.1	4.6	2.5	3.0	3.1	3.6	4.5	4.6	4.9	4.6
Postal and courier services	1.6	9.4	-2.0	2.0	5.1	1.8	9.4	9.7	9.3	9.1
Information and communications	4.1	3.9	3.9	4.6	4.2	3.9	4.5	4.1	4.2	2.9
Financing and insurance	4.2	5.6	4.7	3.6	4.2	4.4	5.4	5.3	5.7	5.9
Real estate, professional and business services	2.8	2.5	1.7	3.5	2.5	3.5	4.2	2.0	2.1	1.6
Real estate	3.5	3.7	0.7	2.8	4.1	6.4	7.9	3.2	1.6	1.9
Professional and business services	2.2	1.4	2.3	4.1	1.1	1.3	0.8	1.0	2.6	1.4
Public administration, social and personal services	2.9	3.2	3.0	3.6	2.7	2.5	2.7	2.9	3.9	3.2

Notes : Figures are subject to revision later on as more data become available.

(a) The GDP figures shown in this table are compiled from the production approach, while those shown in Table 1.1 are compiled from the expenditure approach. For details, see Note (2) to this chapter.

(b) In the context of value-added contribution to GDP, the service sectors include ownership of premises as well, which is analytically a service activity.

(c) Accommodation services cover hotels, guesthouses, boarding houses and other establishments providing short term accommodation.

Other economic developments

1.14 The Financial Secretary, in the 2018-19 Budget, identified three mega trends in the global economy: the unstoppable wave of innovation and technology (I&T), the continued shift in global economic gravity from West to East, and the rising tendency of regional or bilateral trade negotiations between economies amid the threat of protectionism. In response, the Budget pledged to take a proactive approach to ensure that Hong Kong can ride on the enormous opportunities therein through, among other strategies, promoting I&T development in the economy, making bold investments in the future to overcome development bottlenecks posed by land and human capital, and maintaining the competitiveness of our tax regime.

1.15 For the development of I&T, the Budget pledged considerable resources to support the Government's targeted efforts in our areas of strength, namely biotechnology, artificial intelligence, development as a smart city and Fintech, with a view to boosting a diversified economy. In particular, the Budget set aside an additional \$50 billion for developing the Hong Kong-Shenzhen Innovation and Technology Park in the Lok Ma Chau Loop and the Science Park, providing financial support to establish two research clusters in healthcare technologies and in artificial intelligence and robotic technologies, as well as implementing other initiatives that would boost the development of I&T.

1.16 As for investments in the future, the Government will continue to place a high priority on nurturing talent in Hong Kong. The Budget pledged to allocate additional resources in education, training and retraining, which include providing an extra \$2 billion in recurrent expenditure to strengthen support for teachers, kindergartens, integrated education and life-wide learning, as well as a further injection of an additional \$8.5 billion into the Continuing Education Fund, among other initiatives. Separately, the Government will also continue its unwavering efforts to address the development constraints posed by inadequate land supply, through identifying land for housing to boost housing supply and increasing the supply of commercial floor area through various means. For long-term development, the Task Force on Land Supply launched a five-month public engagement exercise in April 2018 to discuss options for increasing land supply.

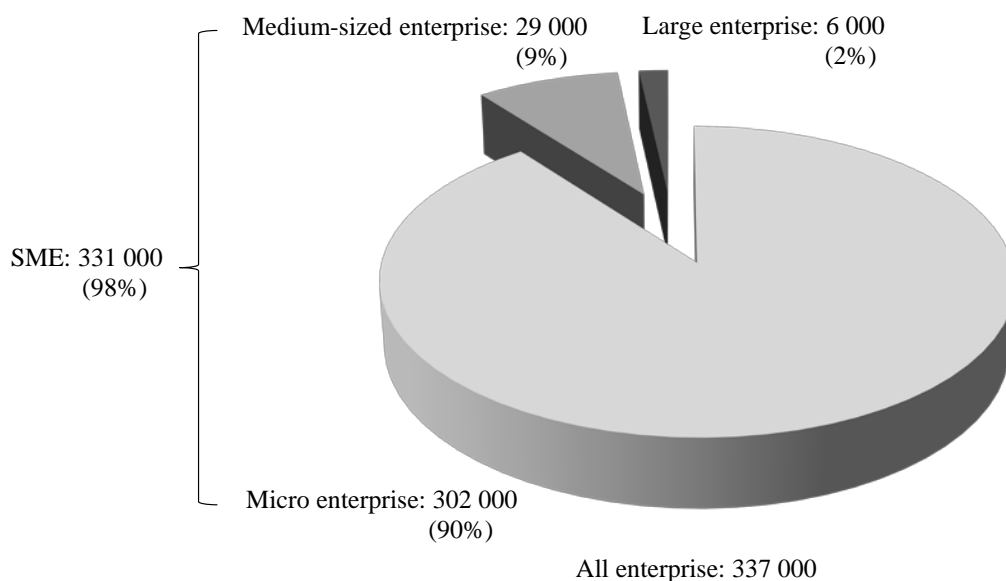
1.17 The Budget also focused on building a caring and sharing society in Hong Kong. In particular, the Budget pledged new resources for initiatives in elderly services, rehabilitation services and child care services. With the substantial fiscal surplus in 2017/18 fiscal year, the Financial Secretary also announced in the Budget various concessionary measures to share the fruits of economic success with the community.

Box 1.2

A snapshot of micro enterprises in Hong Kong

The Hong Kong business sector is predominated by small and medium-sized enterprises (SMEs) which generally refer to enterprises engaging less than 50 persons. In 2017, there were around 331 000 SMEs, accounting for 98% of all enterprises⁽¹⁾ in Hong Kong. Among the SMEs, the number of the so-called micro enterprises, which are defined as those engage less than 10 persons, amounted to some 302 000, representing 90% of all enterprises (*Chart 1*). This proportion has been largely stable over time. Given the sheer number of micro enterprises in the local economy, it is worthwhile to take a closer look at their broad characteristics.

Chart 1: The Hong Kong business sector is predominated by SMEs, especially micro enterprises (2017)



Source: Census and Statistics Department.

General characteristics of micro enterprise

Each micro enterprise, by definition, engages very few persons in its business operation. As such, all micro enterprises together only accounted for around 26% of total employment in the private sector in 2017. According to the Annual Survey of Economic Activities⁽²⁾ in 2016, micro enterprises' share in business receipts was 33% and their share in gross surplus⁽³⁾ was even lower at 16% (*Chart 2*). The overall profit ratio (gross surplus to business receipts) among micro enterprises, at 10%, was also lower than those of medium-sized (engaging 10-49 persons; 19%) and large (engaging 50 or more persons; 27%) enterprises. As for the cost structure, the share of compensation of employees in total operating expenses among micro enterprises tended to be smaller at 28% vis-à-vis 36% among both medium-sized and large enterprises. Characteristics of micro enterprises, nonetheless, may vary across industries.

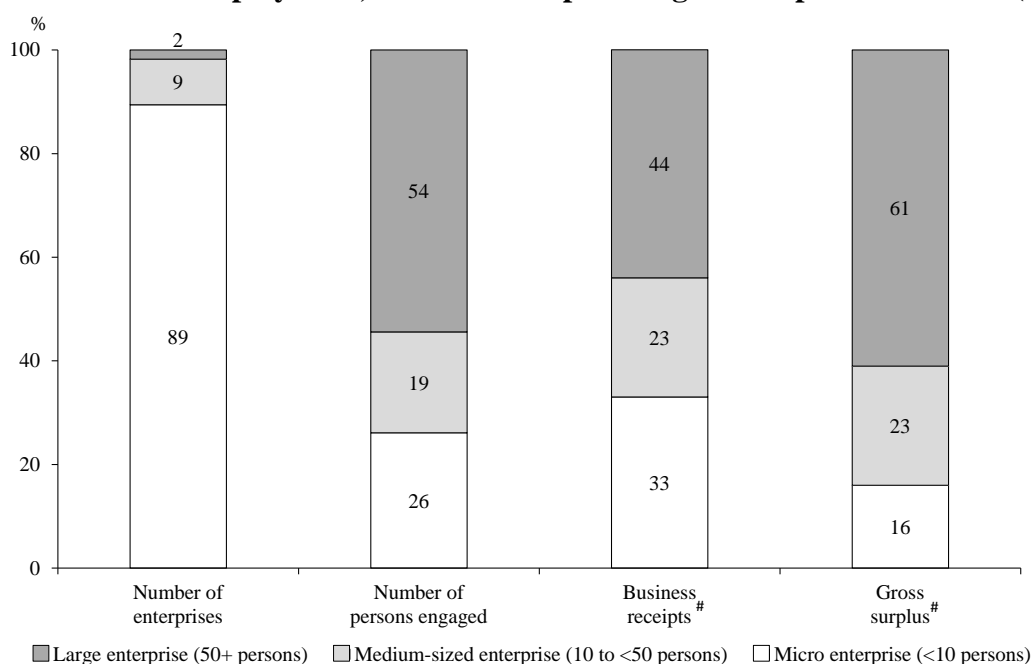
(1) Enterprise here refers to business unit. Establishments with the same main business registration number and engaged in activities of the same industry section are grouped into one business unit for analysis. Figures for the total number of enterprises and total employment exclude civil service and selected economic activities, such as agriculture, forestry and fishing; construction (other than manual workers at construction sites); taxis and public light buses; self-employed insurance agents, authors and artists without business registration; religious organisations; etc.

(2) The figures pertaining to the Annual Survey of Economic Activities in this box article cover the (i) industrial, (ii) transportation, storage and courier services, (iii) import/export, wholesale and retail trades, and accommodation and food services, (iv) information and communications, financing and insurance, professional and business services and (v) building, construction and real estate sectors.

(3) Depreciation and amortisation have been incorporated.

Box 1.2 (Cont'd)

Chart 2: Huge number of micro enterprises but their shares in employment, business receipts and gross surplus were small (2016)



Note: (#) Based on Annual Survey of Economic Activities.

Source: Census and Statistics Department.

General characteristics of micro enterprise by selected industry

While micro enterprises generally dominated the business sector, they featured even more prominently in retail (accounting for 96% of all enterprises in the sector); and wholesale (93%) industries. On the contrary, their shares in financing and insurance (82%); and accommodation and food services (62%) industries were much smaller. The variation should be related to the operational characteristics of different industries. In terms of number, those in import and export trade (29%); retail (18%); and professional and business services (14%) together made up of over 60% of all micro enterprises.

Micro enterprises together accounted for around 26% of total employment in the private sector. Each of these micro enterprises, on average, engaged 3 persons only. Accommodation and food services industry tended to engage more persons per micro enterprise (5 persons) whereas retail; transportation, storage, postal and courier services; and professional and business services industries appeared to engage less (2 persons). The number of employees (i.e. the number of persons engaged excluding working proprietors and partners and unpaid family workers) among micro enterprises averaged only 2. Larger proportion of persons engaged other than employees was seen in retail (53%); and transport, storage, postal and courier services industries (44%), in contrast to import and export trade industry (9%) which was associated with a particularly low ratio.

Other features of micro enterprises

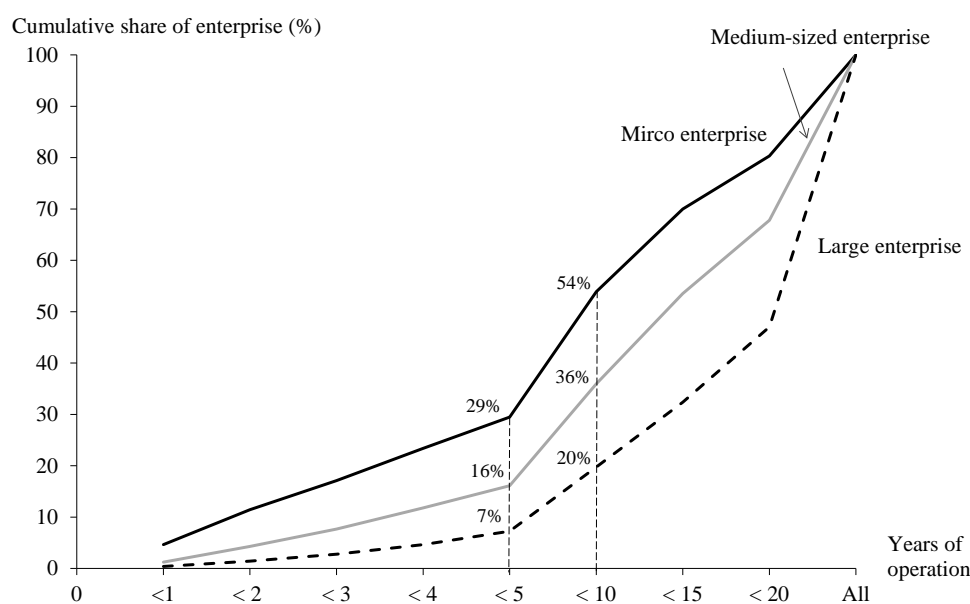
From the distribution of enterprises by year of operation⁽⁴⁾, it is noted that the proportion of enterprises with shorter years of operation was consistently larger among micro enterprises over time. In 2017, 29% of micro enterprises were associated with less than 5 years of operation, while the corresponding share among large enterprises was only 7%. Notwithstanding the above, there was still a notable proportion of micro enterprises (46%)

(4) The number of years of operation of a business unit is derived from the earliest year of commencement among all active establishments under the business unit. The year of commencement of individual establishment is primarily based on the information on commencement date or business registration date as recorded by the Business Registration Office.

Box 1.2 (Cont'd)

having operated for 10 years or more. It appears that a substantial share of micro enterprises is likely to remain small for a long period of time (*Chart 3*).

Chart 3: Larger proportion of young enterprises among micro enterprises (2017)



Source: Census and Statistics Department.

In fact, enterprise usually starts with a small scale. Between 2012 and 2017, around 95% of new enterprises coming into operation each year were micro enterprises, probably because starting small can somehow reduce the business risks. At the same time, around 94% of the enterprises ceasing operation were micro enterprises. This may be attributable to various reasons. For instance, micro enterprises could be more vulnerable in staying afloat and some enterprises may have reduced their scale of operation before ceasing business. These incoming and outgoing enterprises made up of around 11% and 10% of all micro enterprises each year respectively. The larger share of incoming and outgoing enterprises among micro enterprises may have affected the overall profit ratio among them.

By tracking the micro enterprises which commenced operation in 2012 for a five-year period, it was found that only around half of them remained in operation by 2017. Their “survival” rate was lower than those commenced as medium-sized (around 60%) and large (around 75%) enterprises. Around a quarter of the micro enterprises which started operation in 2012 ceased to operate within the first two years. The “drop-out” rate moderated during the course of the five-year period, lowering to around 5% in the fifth year of operation. Comparing with medium-sized and large enterprises, micro enterprises were seen to be “dropping out” at a more rapid rate than their counterparts.

Among those micro enterprises which commenced operation in 2012 and stayed in operation in 2017, a tiny proportion (less than 5%) of them did grow bigger and turned into medium-sized/large enterprises by 2017. Though nearly all of the micro enterprises which stayed in operation remained as micro enterprises after five years of operation, around 20% of them in fact expanded in terms of number of persons engaged.

Micro enterprises vary greatly among themselves

The snapshot above shows that while there are common features among micro enterprises, their characteristics can vary due to many factors, including the industry in which they are engaging, whether they are new start-ups, whether they are about to wind down, and/or whether they are long-established enterprises which can survive with their own business model.

Notes :

- (1) The global economic growth forecasts for 2018 by the IMF in April 2018 mainly consisted of an improved outlook for advanced economies and sustained solid growth for the Mainland. The table below presents a more detailed comparison between the growth forecasts made by the IMF in April 2018 and those three months ago.

	<u>2017</u>	<u>2018</u>	
	(%)	<u>January round</u> (%)	<u>April round</u> (%)
World (PPP ^{##} weighted)	3.8	3.9	3.9
Advanced economies	2.3	2.3	2.5
US	2.3 [#]	2.7	2.9
Euro area	2.4 [#]	2.2	2.4
UK	1.8 [#]	1.5	1.6
Japan	1.7 [#]	1.2	1.2
Emerging market and developing economies	4.8	4.9	4.9
Emerging and developing Asia	6.5	6.5	6.5
Mainland China	6.9 [#]	6.6	6.6
India [^]	6.6 [#]	7.4	7.4
Middle East and North Africa ⁺	2.6	3.6	3.4

- Notes : (#) Actual figures.
 (##) PPP refers to purchasing power parity.
 (^) Fiscal year.
 (+) Based on “Middle East, North Africa, Afghanistan, and Pakistan” as defined by the IMF.

- (2) The Gross Domestic Product (GDP) is an overall measure of net output produced within an economy in a specified period, such as a calendar year or a quarter, before deducting the consumption of fixed capital. In accordance with the expenditure approach to its estimation, GDP is compiled as total final expenditures on goods and services (including private consumption expenditure, government consumption expenditure, gross domestic fixed capital formation, changes in inventories, and exports of goods and services), less imports of goods and services.
- (3) The seasonally adjusted quarter-to-quarter GDP series, by removing the variations that occur at about the same time and in about the same magnitude each year, provides another perspective for discerning the trend, particularly in regard to turning points. A detailed examination reveals the presence of seasonality in the overall GDP and in some of its main components, including private consumption expenditure, government consumption expenditure, exports of goods, imports of goods, exports of services, and imports of services. However, due to the presence of considerable short-term fluctuations, no clear seasonal pattern is found in gross domestic fixed capital formation. Therefore, the seasonally adjusted series of GDP is compiled separately at the overall level, rather than summing up from its main components.