



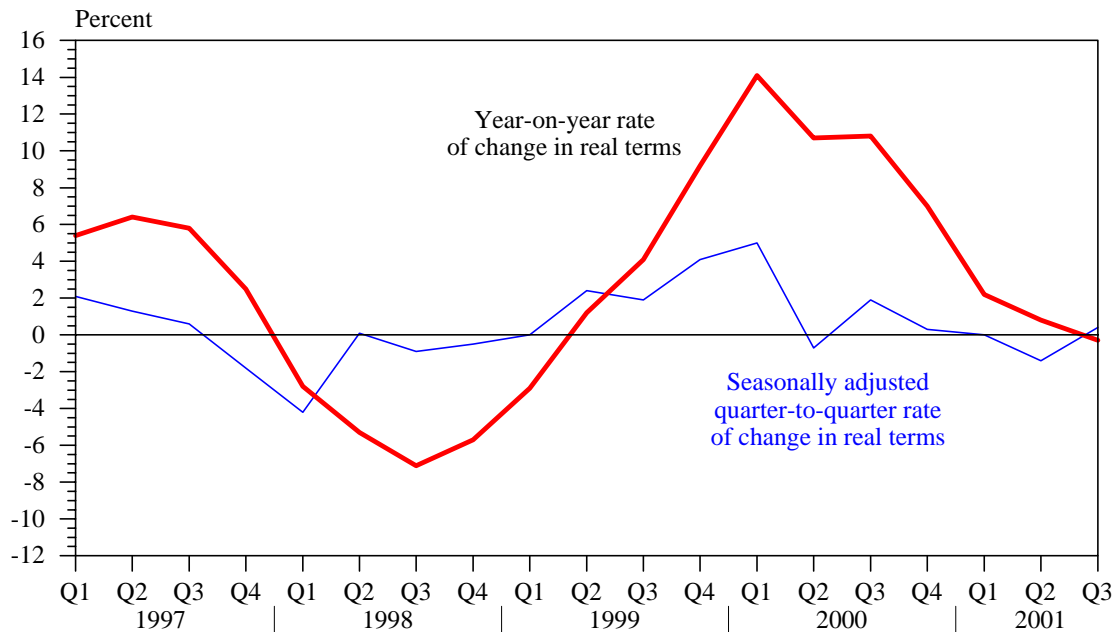
## **Hong Kong's recent economic situation and short-term outlook**

The Government has just released the Third Quarter Economic Report 2001 at the end of last month. The Economic Report, together with the press release containing the updated economic forecasts for 2001 as a whole, have been furnished to LegCo Members.

This paper first analyses Hong Kong's overall economic growth and the developments in regard to external trade, domestic demand, labour market, consumer prices and financial markets in the recent period. It then provides a brief account on the Government's updated economic forecasts for 2001 as a whole, followed by some initial views on the economic outlook for 2002.

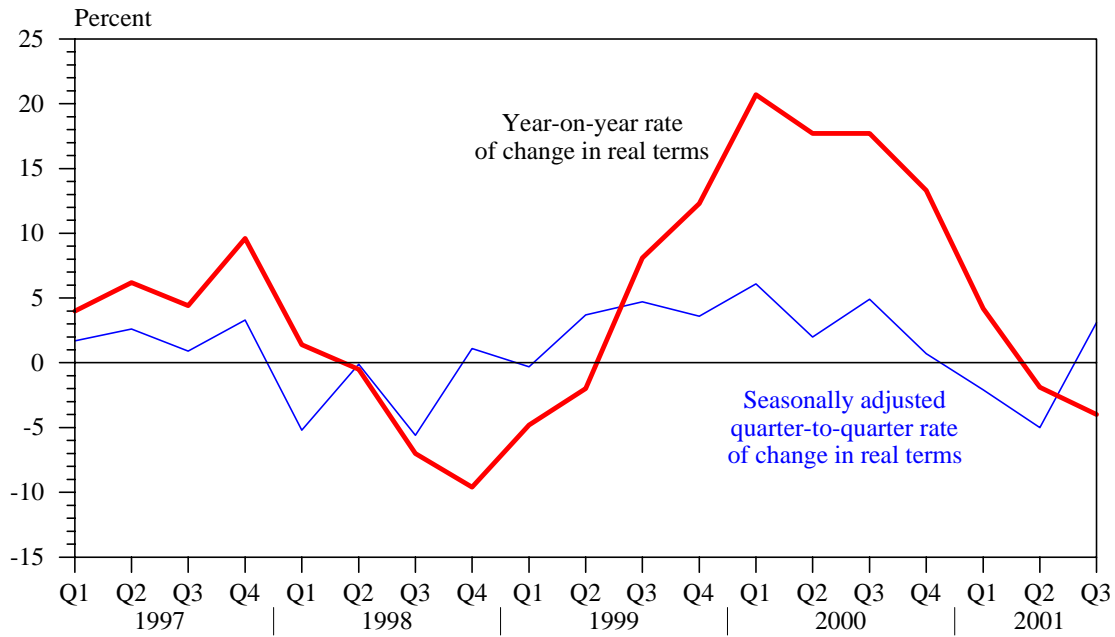
1 December 2001

**Chart 1 : Hong Kong's Gross Domestic Product**



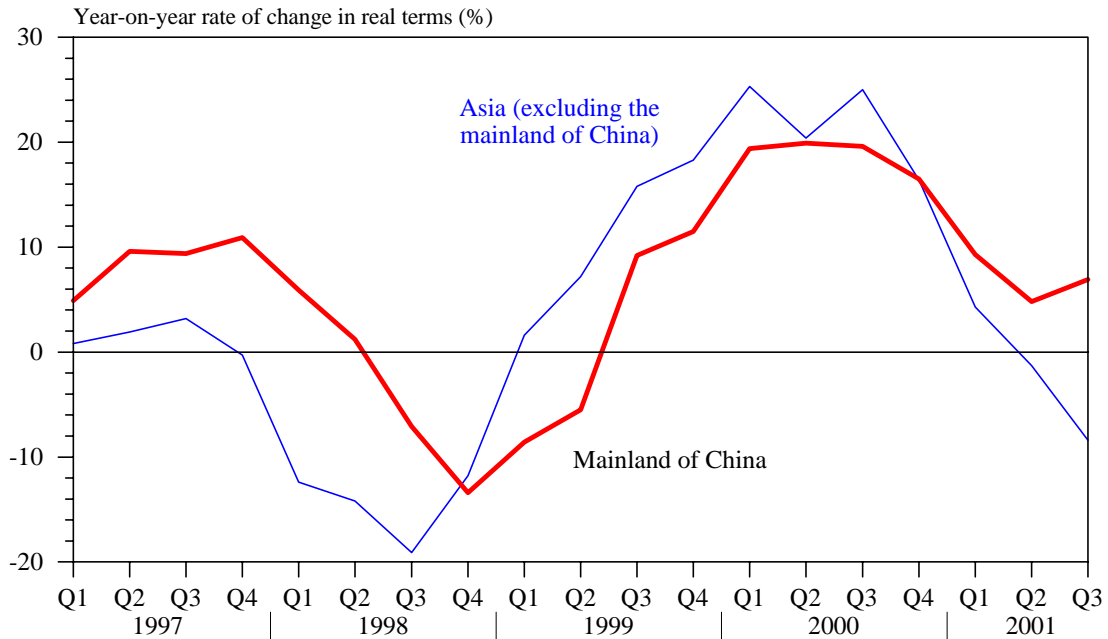
- Affected by the global economic downturn, the Hong Kong economy had been slackening since the beginning of this year. The external environment worsened even more in the aftermath of the 911 incident.
- The protracted slump in external demand had resulted in an enlarged decline in exports, while local consumption also weakened amidst the deterioration in employment conditions.
- On a year-on-year comparison, the Gross Domestic Product (GDP) slackened further to a slight decline of 0.3% in real terms in the third quarter of 2001, down from a 0.8% growth in the second quarter.
- Yet on a seasonally adjusted quarter-to-quarter comparison, GDP rose back by 0.4% in real terms in the third quarter, after declining by 1.4% in the second quarter.

**Chart 2 : Hong Kong's total exports of goods**



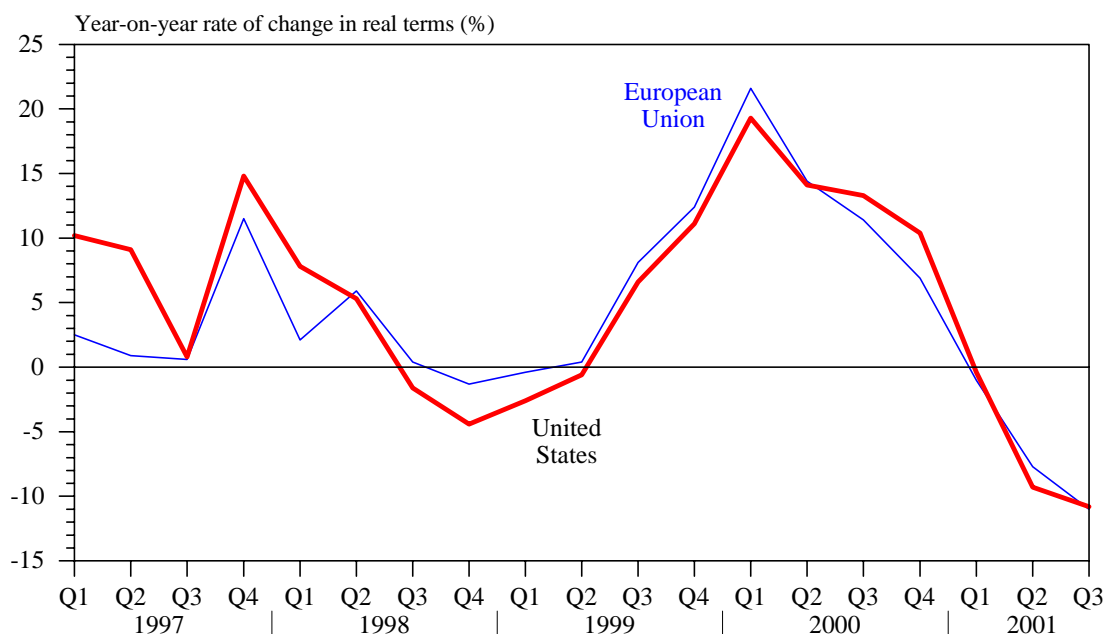
- On visible trade, exports remained sluggish amidst an across-the-board setback in import intake in the major conventional markets and a slump in intra-regional trade. The decline in total exports of goods enlarged to 4% in real terms in the third quarter of 2001, and to around 11% in October.

**Chart 3 : Hong Kong's total exports of goods to Asia**



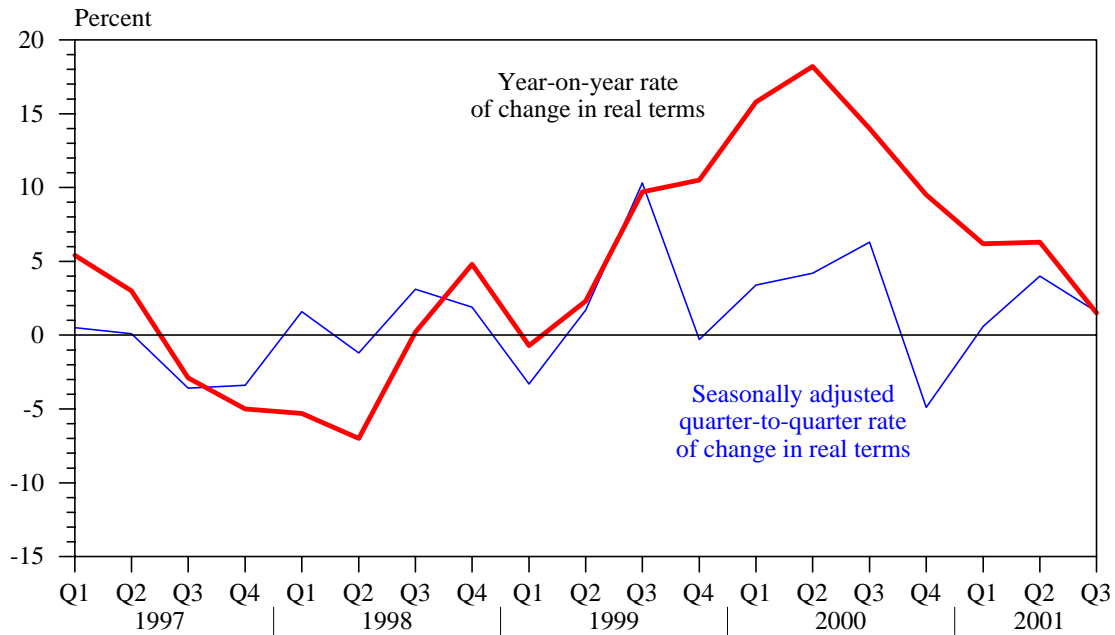
- Over half of Hong Kong's merchandise exports are destined to Asia, of which around two-thirds are destined to the mainland of China.
- Underpinned by the sustained robust economic growth in the Mainland, exports of goods to the Mainland still held up well in the third quarter of 2001, rising by 7% in real terms over a year earlier.
- On the other hand, Hong Kong's exports of goods to most of the other Asian economies plunged sharply, with exports to Taiwan plummeting by 19% in real terms, exports to Singapore even more, by 20%, and exports to the Republic of Korea by 9%.

**Chart 4 : Hong Kong's total exports of goods to the United States and the European Union**



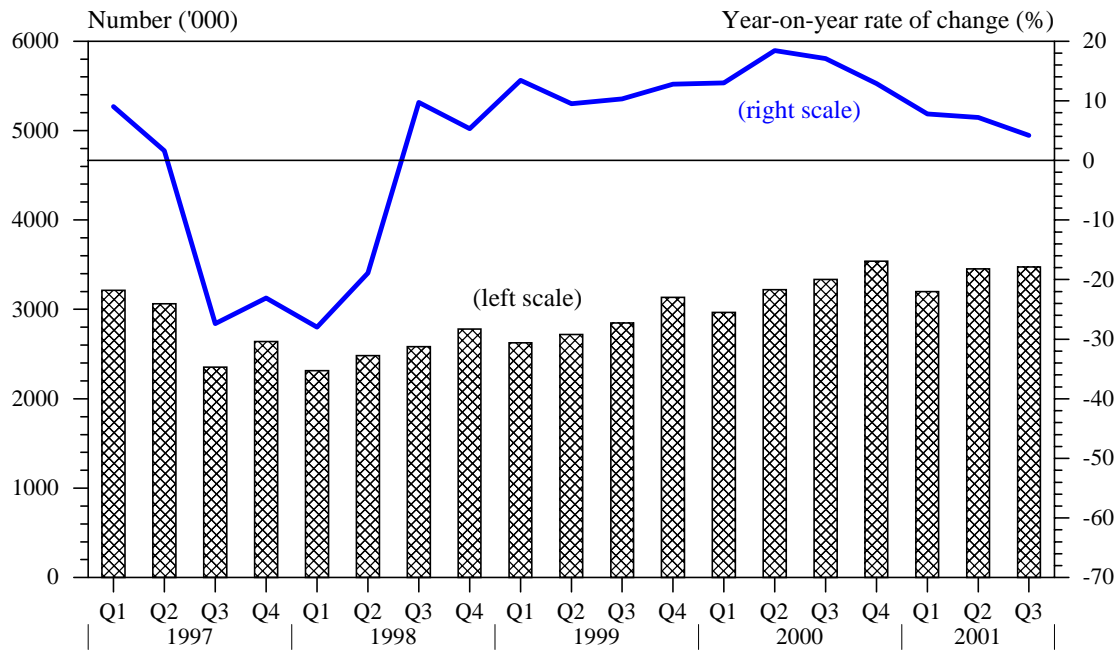
- As to the other major conventional markets, affected by worsening economic conditions in the United States, Hong Kong's exports of goods to this market plummeted by 11% in real terms in the third quarter of 2001 over a year earlier.
- Over the same period, exports to the European Union also plunged by 11% in real terms, along with the visible slow-down in the EU economy, and with the weakness of the euro concurrently curtailing import demand in this region.

**Chart 5 : Hong Kong's exports of services**



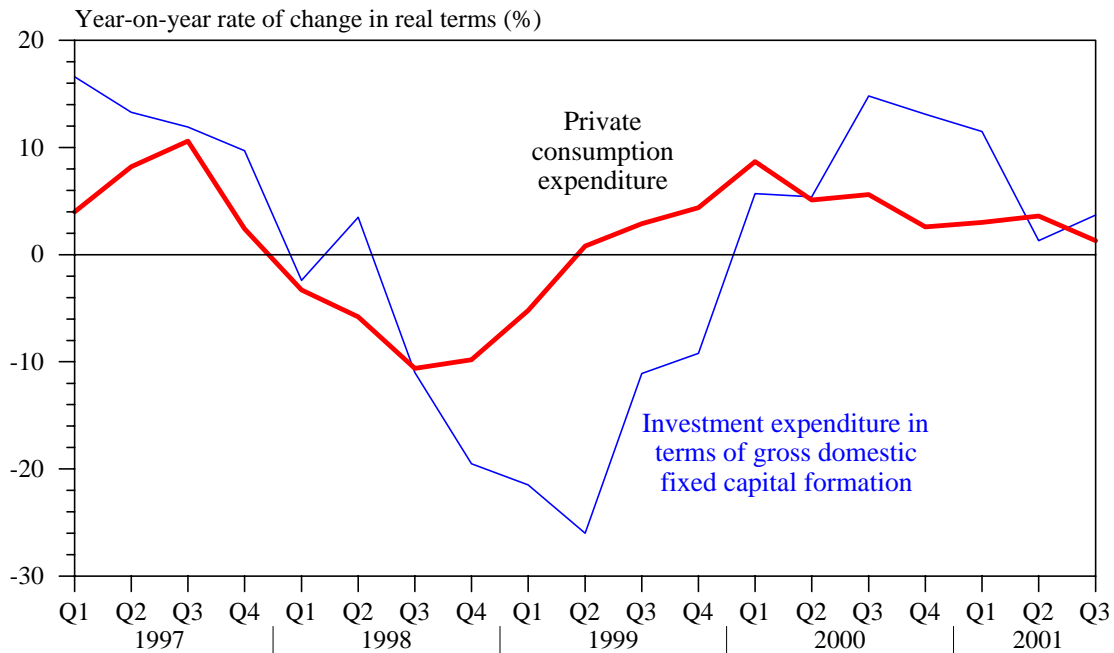
- On invisible trade, exports of services were likewise affected by the global economic downturn. The 911 incident had caused a distinct setback in inbound tourism, hence exacerbating the performance of exports of services further.
- Exports of services thus slowed to a meagre growth of 1.5% in real terms in the third quarter of 2001 over a year earlier.

**Chart 6 : Visitor arrivals to Hong Kong**



- For July and August combined, the number of incoming visitors still had a 7% growth over a year earlier. However, with inbound tourism being hard hit in the wake of the 911 incident, visitor arrivals fell off distinctly in September and October, with respective declines of 2% and 3%.

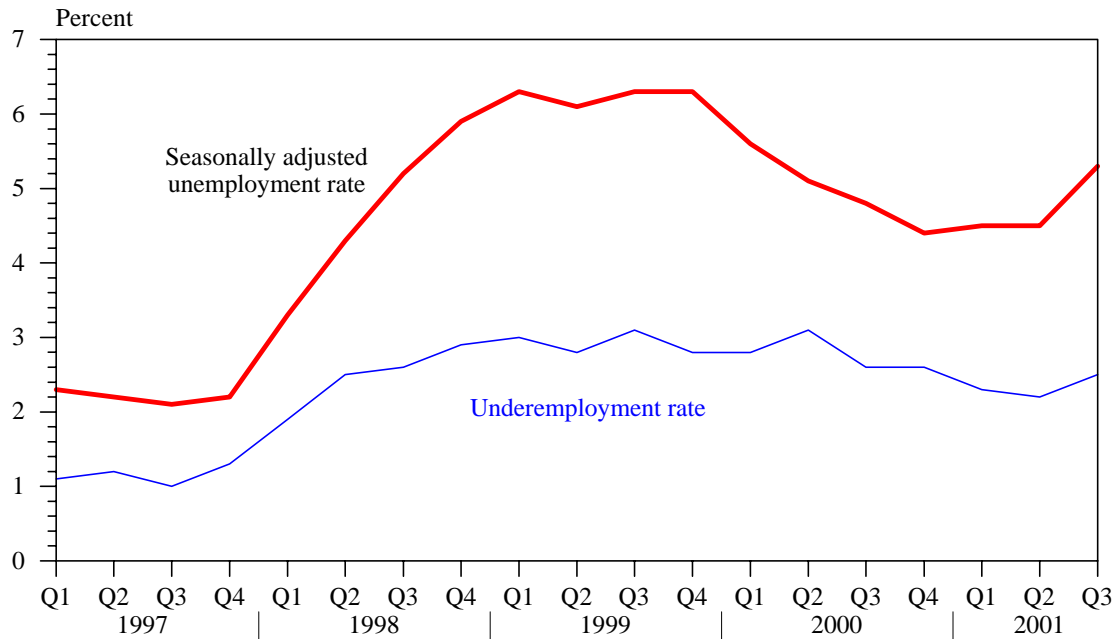
**Chart 7 : Hong Kong's domestic demand**



- Affected by worsening employment conditions, private consumption expenditure slackened distinctly in the third quarter of 2001, to a mere growth of 1.3% in real terms over a year earlier.
- Overall investment spending, having eased back markedly in the second quarter of 2001, had a somewhat better performance in the third quarter, with a growth of 3.7% in real terms over a year earlier. This was due to the delivery of aircraft ordered earlier, thereby boosting the expenditure on machinery and equipment in that quarter.
- On the other hand, with the heavy scale-back in the Public Housing Programme, coupled with a dearth of new building projects in the private sector, building and construction output remained sluggish in the third quarter of 2001.

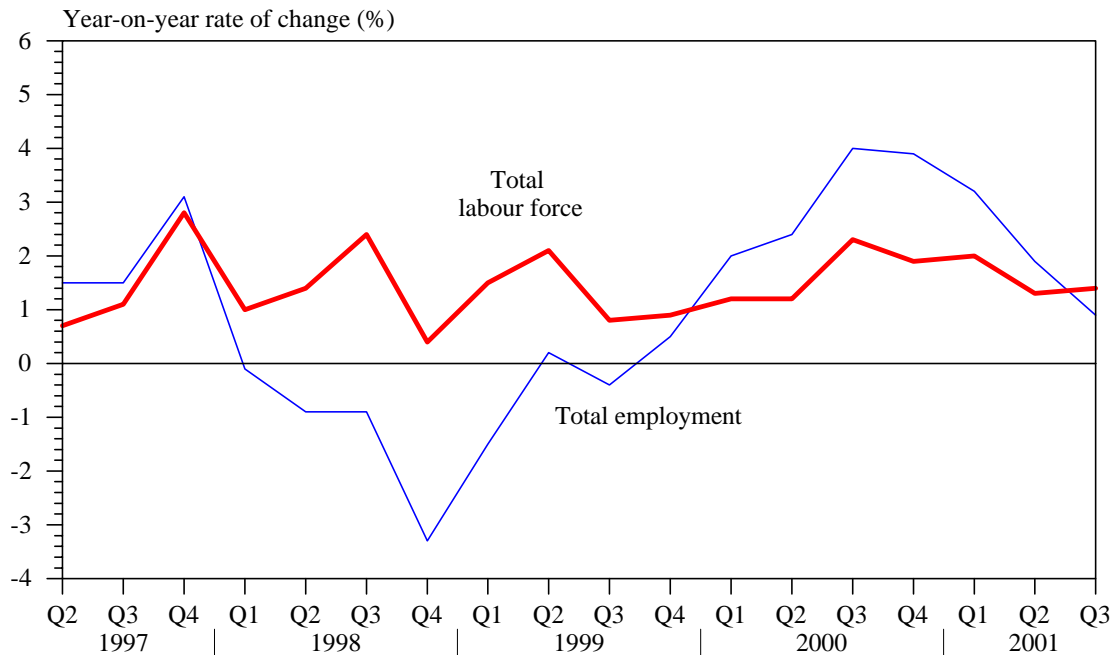


**Chart 8 : Unemployment and underemployment rates**



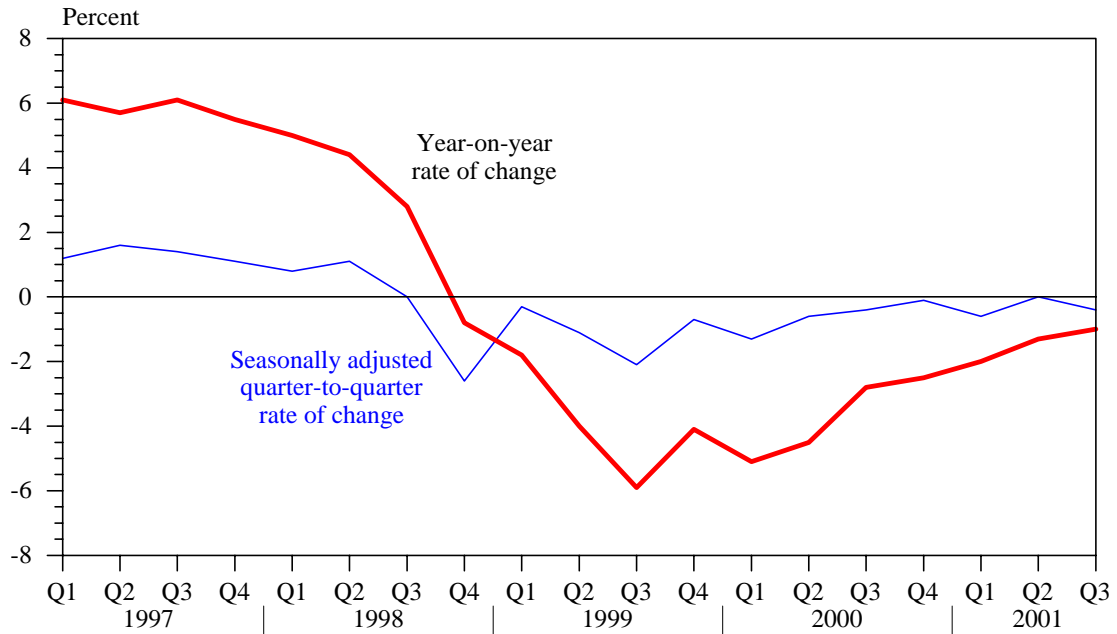
- The labour market also slackened, with the seasonally adjusted unemployment rate surging from 4.5% in the second quarter of 2001 to 5.3% in the third quarter, and to 5.5% in the period August to October.
- The underemployment rate likewise went up, from 2.2% in the second quarter of 2001 to 2.5% in the third quarter, and to 2.6% in the period August to October.

**Chart 9 : Total labour force and total employment**



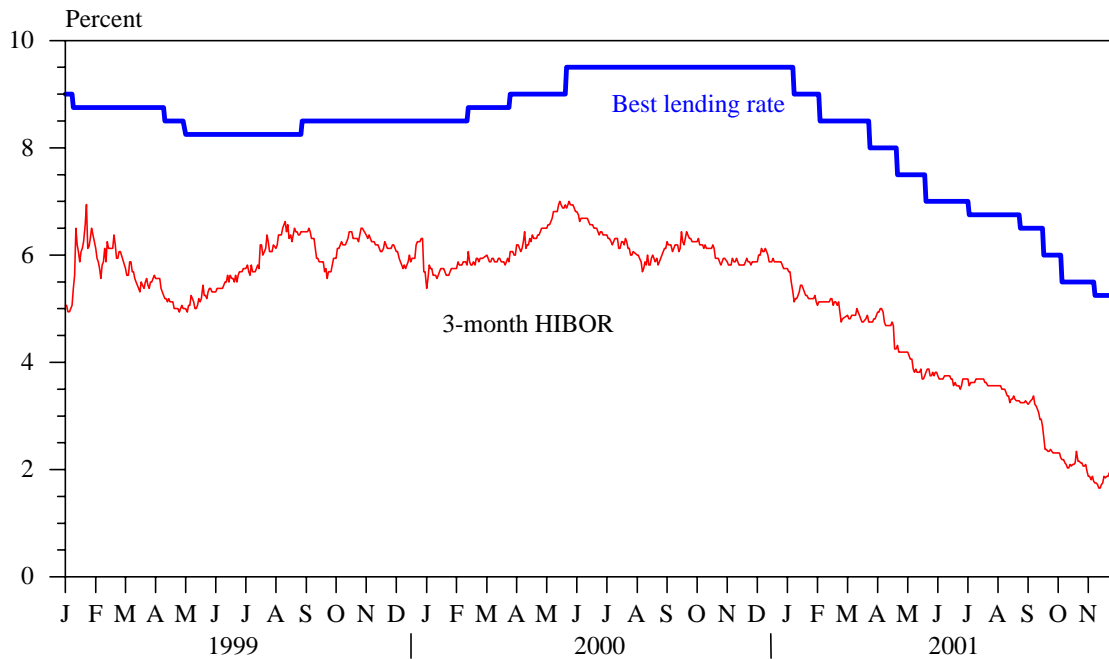
- Labour demand had continued to ease since the beginning of this year, along with the downturn in the overall economy. Corporate downsizing and lay-offs continue to occur, particularly after the 9/11 incident.
- In the third quarter of 2001, growth in labour demand was unable to catch up with growth in the labour force, for the first time since end-1999, leading directly to a surge in unemployment rate in that quarter.

**Chart 10 : Composite Consumer Price Index**



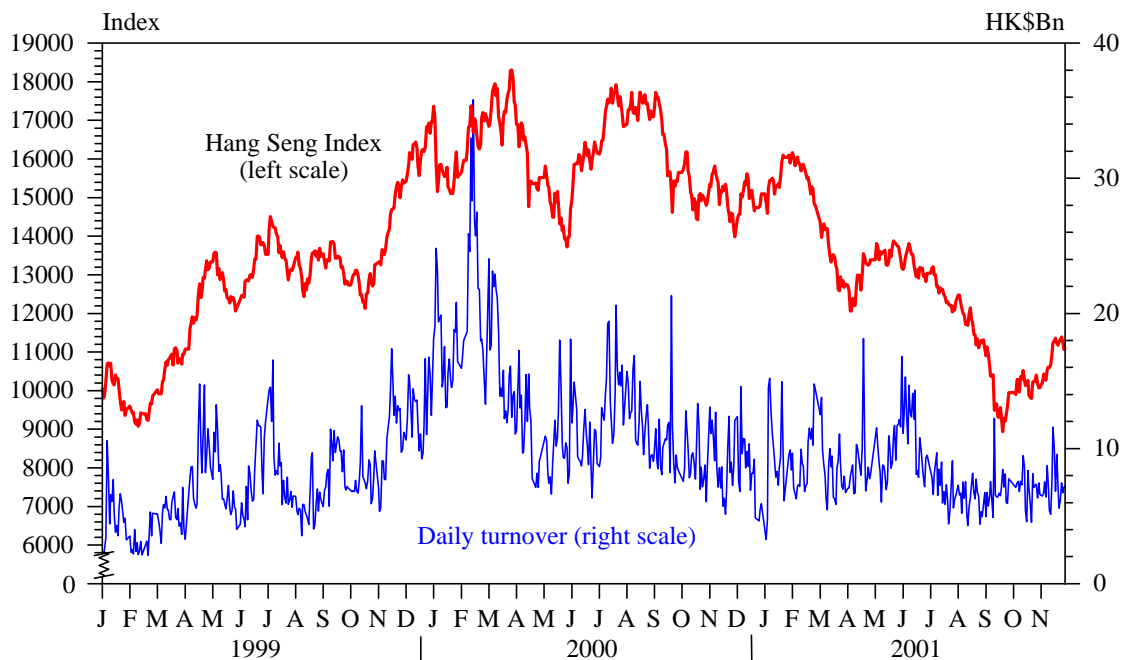
- The Composite CPI still had a 1.4% decline in the first ten months of 2001 over a year earlier, amidst the easing in local costs, the earlier strength of the US dollar, and the fall-off in world commodity prices.

**Chart 11 : Interest rates in Hong Kong**



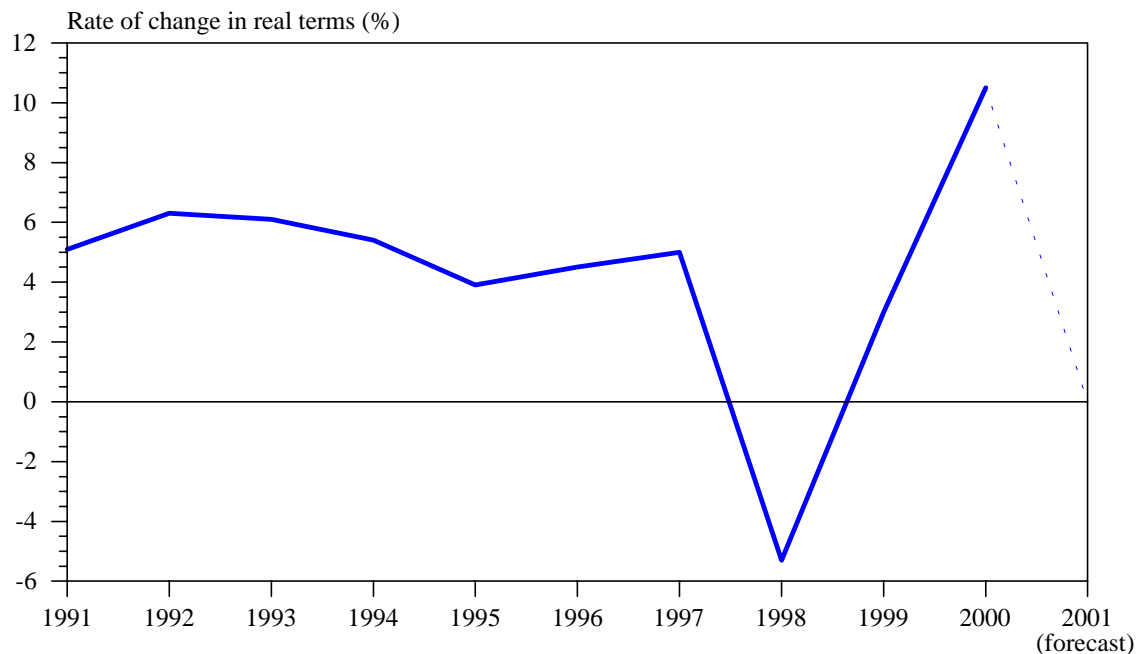
- Following successive cuts in US interest rates, local interest rates were down by 4.25 percentage points so far this year, with the best lending rate now at a 13-year low.

**Chart 12 : Hang Seng Index and Hong Kong's stock market turnover**



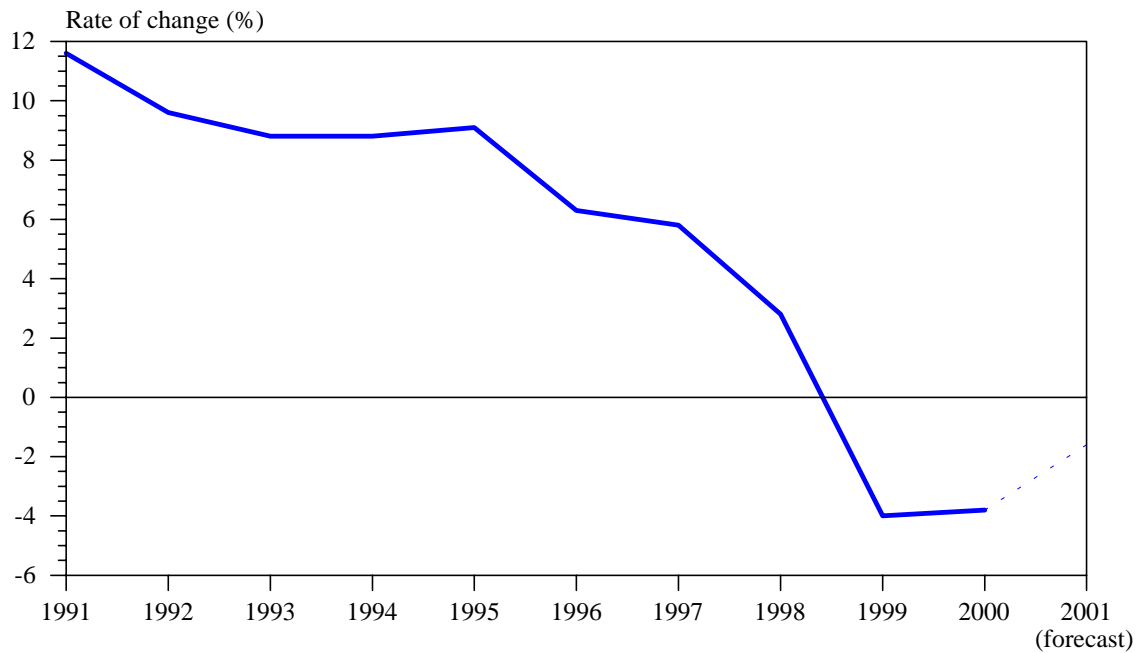
- Along with the setback in stock markets overseas, the local stock market had tended to weaken even before the 911 incident.
- Then, the sharp plunge in the global financial markets in the wake of the 911 incident caused the Hang Seng Index to plummet to a low of 8 934 on 21 September. As gyrations in stock markets overseas gradually settled, the Hang Seng Index also rose back, to 9 951 at the end of the third quarter, though still 24% lower than the level at the end of the second quarter.
- With the further cuts in interest rates recently, coupled with the rally in the US stock market, the Hang Seng Index rebounded more notably in November, surpassing the 11 000 mark on 15 November. It closed the month at 11 279.

**Chart 13 : Forecast of Hong Kong's Gross Domestic Product for 2001**



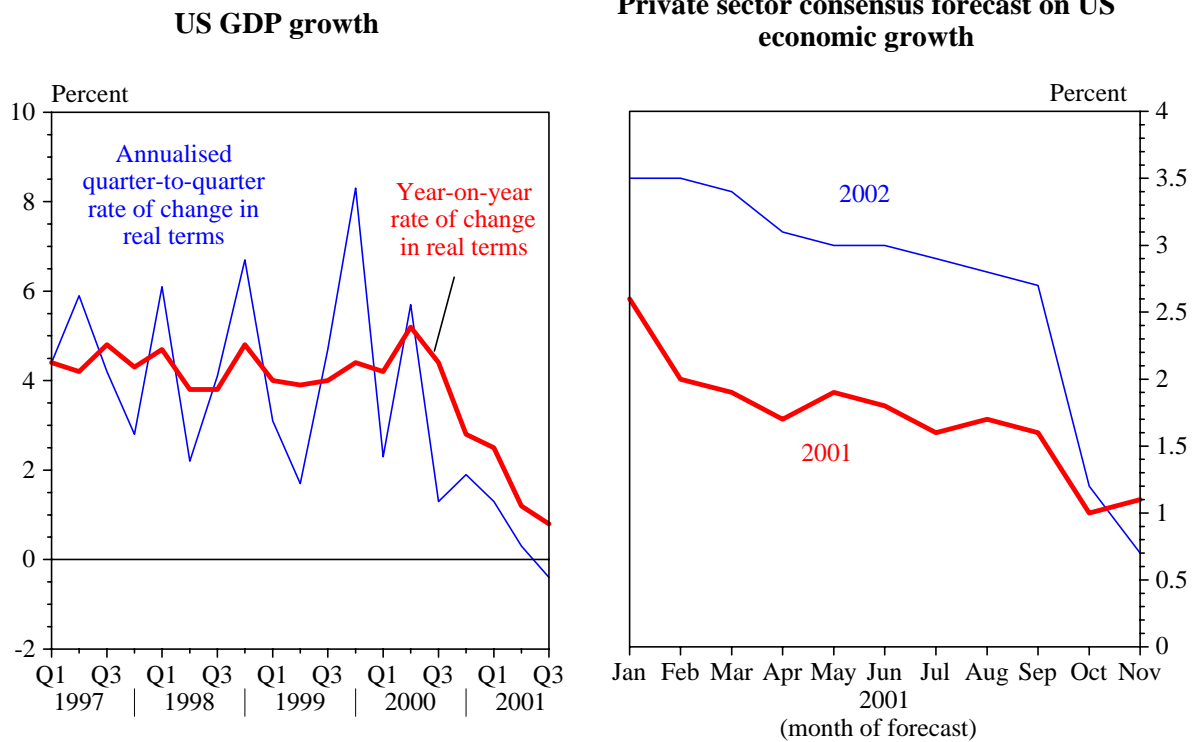
- With the 911 incident inflicting considerable negative impact on the global economy, Hong Kong as a small and externally oriented economy is bound to be hit.
- After appraising the latest developments on the external and local fronts, the Government has lowered further the GDP forecast for 2001 as a whole to zero growth, from the forecast of 1% growth put out earlier.

**Chart 14 : Forecast of Hong Kong's Composite Consumer Price Index for 2001**



- As local business costs have tended to ease in the recent period, and as import prices have also come down more distinctly, the decline in consumer prices is likely to protract further.
- Together with the mitigating effect on consumer prices that will be brought about by the waiver of public housing rentals in December, the Government now envisages the decline in consumer prices for 2001 as a whole to average at 1.6%.

**Chart 15 : US economy**

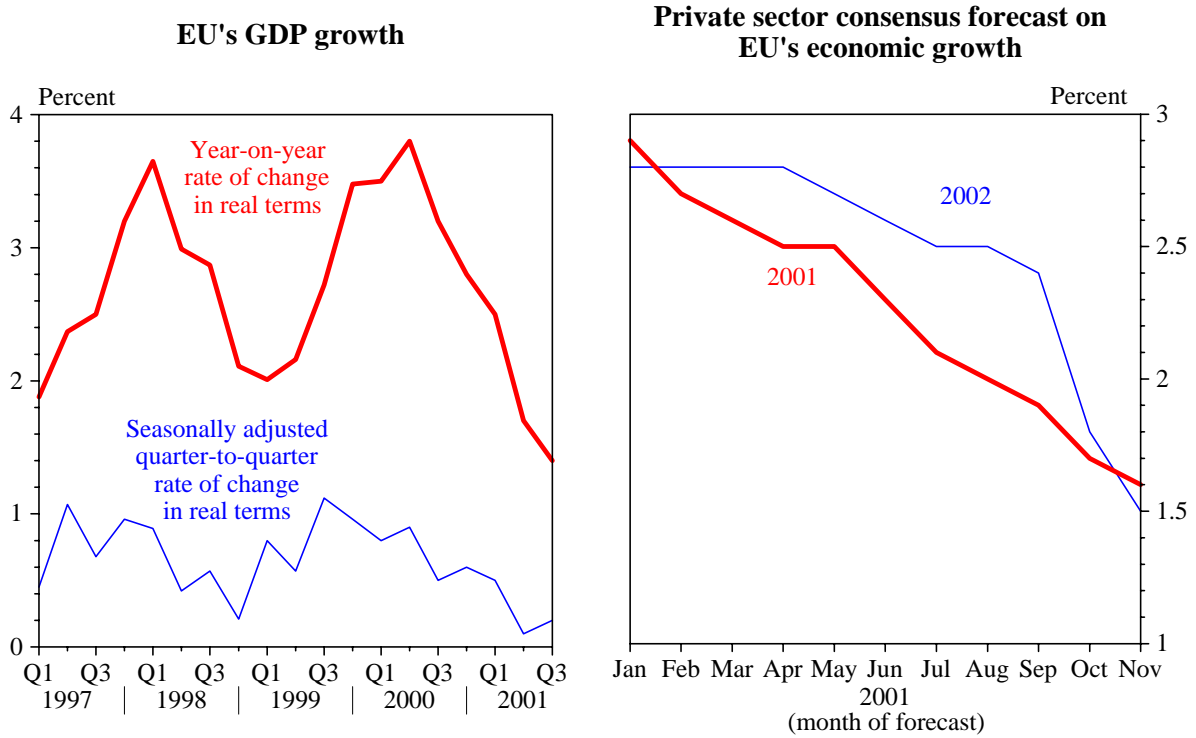


Looking ahead into 2002 :

- With the severe shock inflicted on the US economy by the 911 incident, international organisations and private sector analysts generally expect the US economy to slow down further, to a 0.7% growth in 2002, from the 1.1% growth in 2001.
- Broadly speaking, the recovery process in the US economy is inevitably being delayed and retarded, making the near-term outlook all the more uncertain.

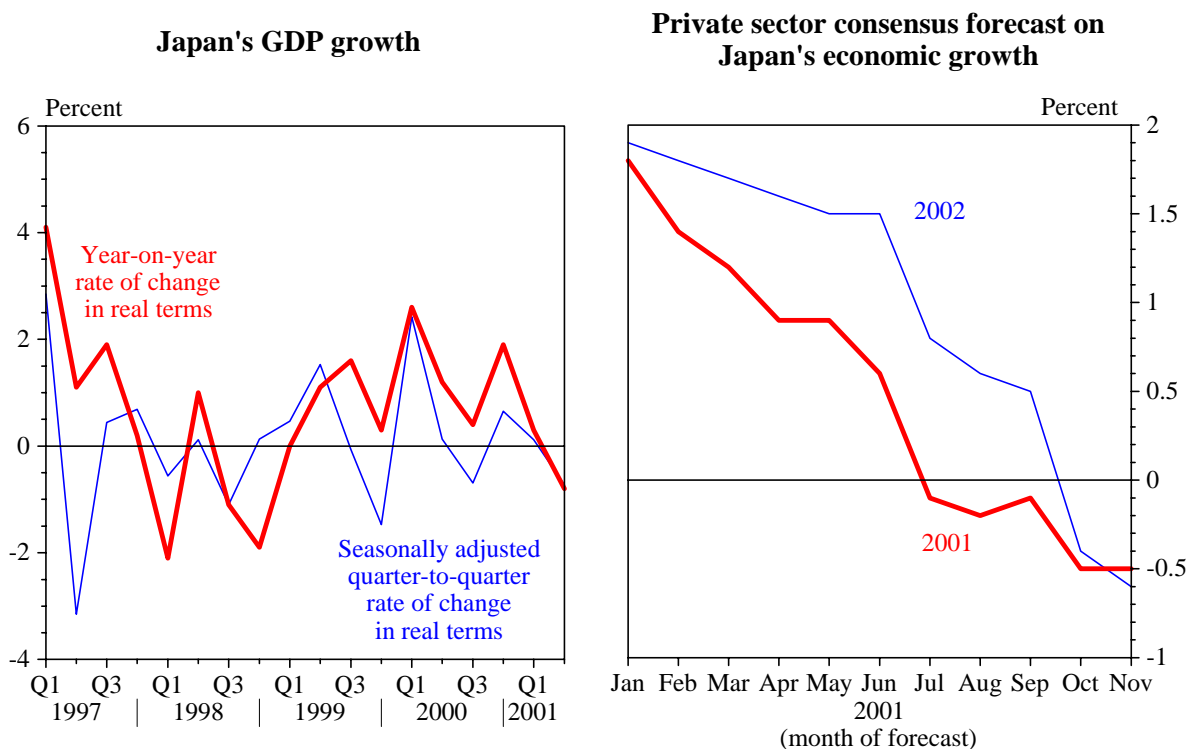


**Chart 16 : EU economy**



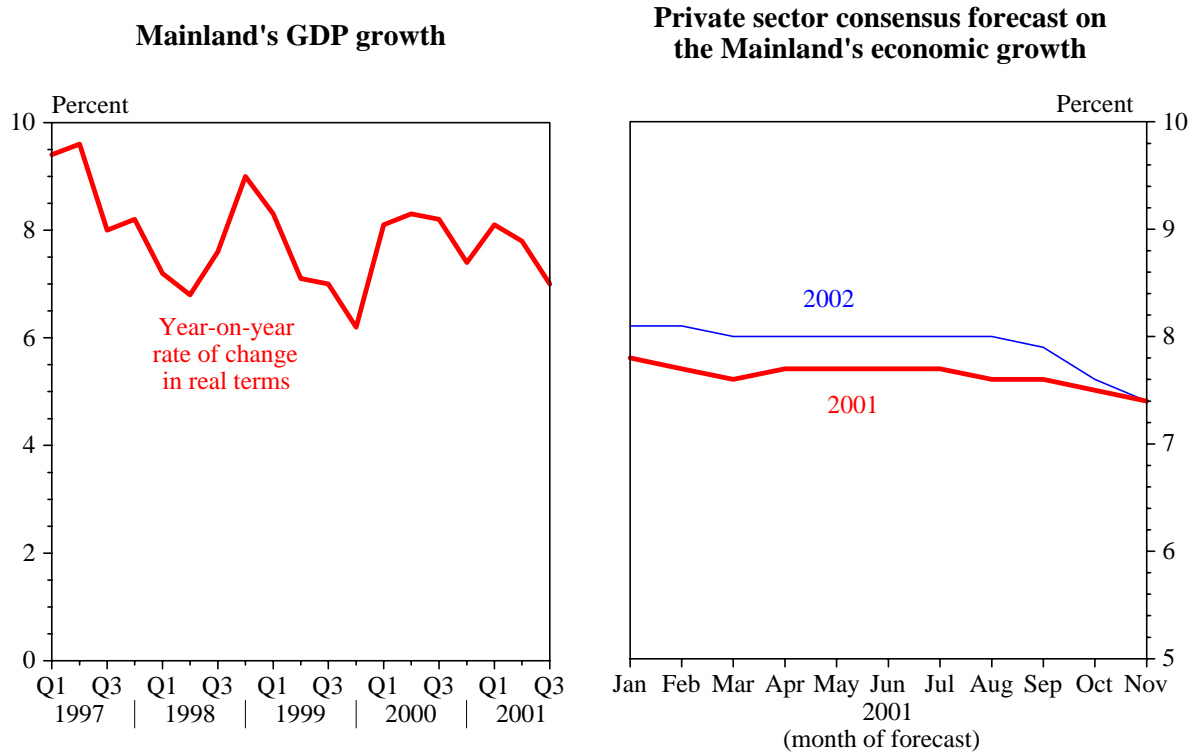
- Given the close trade and investment links between the United States and the European Union, the US economic downturn has led to a visible slow-down in the EU economy.
- In the wake of the 911 incident, international organisations and private sector analysts have also marked down the forecast growth in the EU economy to 1.4-1.5% in 2002, slightly below that of 1.6-1.7% in 2001.

**Chart 17 : Japan's economy**



- The Japanese Government has progressively lowered its assessment of Japan's economy in the course of this year. Most recently, it has revised the forecast growth for 2001 as a whole down to -0.9%, from that of 1.7% put out earlier.
- The Bank of Japan and private sector analysts expect Japan's economy to continue to shrink in 2002, that is, to have two consecutive years of negative growth.

**Chart 18 : Mainland's economy**



- Notwithstanding the austere global economic environment, the economy of the mainland of China has continued to put up a robust growth in the recent period.
- While the Mainland's exports are likewise affected by the slump in global demand, its buoyant domestic demand should continue to render a strong impetus to growth. This can be expected to underpin its overall economic growth at around 7% in 2002.

### Short-term outlook for the Hong Kong economy :

- Overall economic conditions will remain difficult in the near term, and a recovery in the early part of 2002 seems unlikely.
- In the local economy, private consumption expenditure looks set to slow down further upon the rising unemployment, while investment spending is likely to remain slack amidst an uncertain business outlook.
- Despite the gloomy situation in the short term, the medium and longer term outlook for Hong Kong's economic development is good. The Mainland economy will continue to be bolstered by implementation of the 10th Five-year Plan and by China's accession to WTO, which in turn will generate more business opportunities for Hong Kong. In addition, the HKSAR Government's substantial investment in human resources and physical infrastructure, coupled with the on-going drive to enhance the overall business environment, are also conducive to Hong Kong's economic development in the longer term.