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Hong Kong's Recent Economic Situation and Near-term Outlook

The Government released the Third Quarter Economic Report 2017 on 10 November 2017. The Economic Report, together with the press release containing the updated economic forecasts for the whole year of 2017, have been furnished to LegCo Members.

This paper analyses Hong Kong's overall economic development in the most recent period as well as outlook in the near term, and provides some preliminary analysis on the outlook in 2018.

Economic Analysis and Business Facilitation Unit
Financial Secretary's Office
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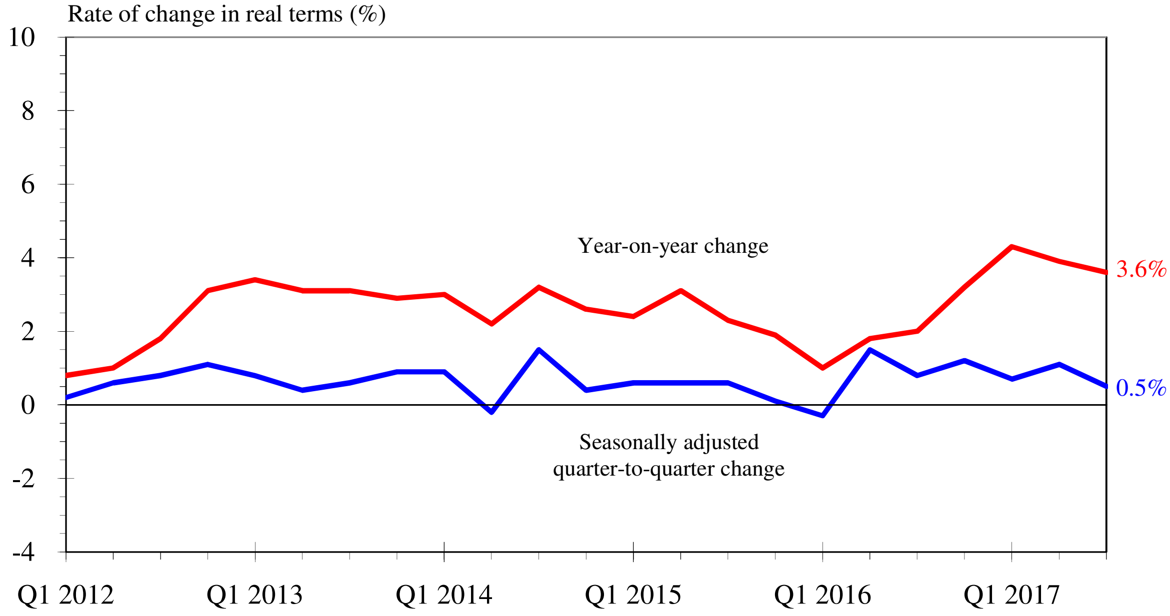
Introduction

This paper analyses the recent development in the Hong Kong economy, and provides some preliminary analysis on the outlook in 2018.

Recent economic situation

2. The Hong Kong economy continued to expand notably in the third quarter of 2017, by 3.6% over a year earlier(1). This marked the fourth consecutive quarter of above-trend growth. External demand stayed vibrant, whereas domestic demand attained solid growth. On a seasonally adjusted quarter-to-quarter comparison, real GDP grew by 0.5% in the third quarter of 2017 ***(Chart 1)***. In the first three quarters of 2017 combined, the economy grew by 3.9% over a year earlier.

Chart 1 : The Hong Kong economy continued to show an above-trend growth in the third quarter of 2017



(1) Unless specified, all figures in the sections of Recent economic situation, External trade and Domestic sector in this document refer to year-on-year change in real terms.

External trade

3. The global economy stayed benign in the third quarter of 2017. The US economy expanded at a moderate pace. The ongoing economic recovery in the euro area has become more entrenched. Against these positive developments, the Federal Reserve (the Fed) began trimming its balance sheet in October 2017, and the European Central Bank (ECB) also announced to reduce its monthly asset purchases starting from early 2018. Meanwhile, the Mainland economy sustained medium-high speed growth. Besides, regional trading and manufacturing activities continued to be vibrant in Asia. Acknowledging the progress made in the global economy in 2017, the International Monetary Fund (IMF) in October revised up its global economic growth forecast for 2017 to 3.6%, representing a pick-up from the 3.2% growth in 2016.

4. Benefitting from the general economic upturn of major economies, Hong Kong's total exports of goods maintained notable growth of 5.5% in the third quarter of 2017 ***(Chart 2(a))***. With reference to external merchandise trade statistics in the third quarter of 2017, Hong Kong's exports to Asian markets as a whole outperformed those to the other regions, thanks to sustained growth in demand for raw materials, semi-manufactures and capital goods amid vibrant manufacturing activities in the region. On a year-on-year comparison in real terms, exports to the Mainland picked up to show notable growth. Exports to Taiwan, Singapore and Japan all attained double-digit growth, and those to India also grew notably. Exports to the EU picked up somewhat to show visible growth for the third quarter of 2017 as a whole, whereas those to the US continued to lag behind by comparison. The external trade performance stayed solid on entering the fourth quarter of 2017, with merchandise exports rising by 7.3% in value terms over a year earlier in October and November 2017 combined.

5. Exports of services picked up to grow by 3.7% in the third quarter of 2017, from the 2.6% growth in the preceding quarter ***(Chart 2(b))***, reflecting vibrant regional trade and cargo flows and the recovery of inbound tourism. Within exports of services, exports of travel services resumed moderate growth after declining for over three years. Inbound tourism saw further recovery on entering the fourth quarter of 2017, with the number of visitor arrivals picking up to show a year-on-year growth of 6.8% in October and November 2017 combined, compared with the 1.8% growth in the third quarter.

Chart 2(a) : Total exports of goods maintained notable growth

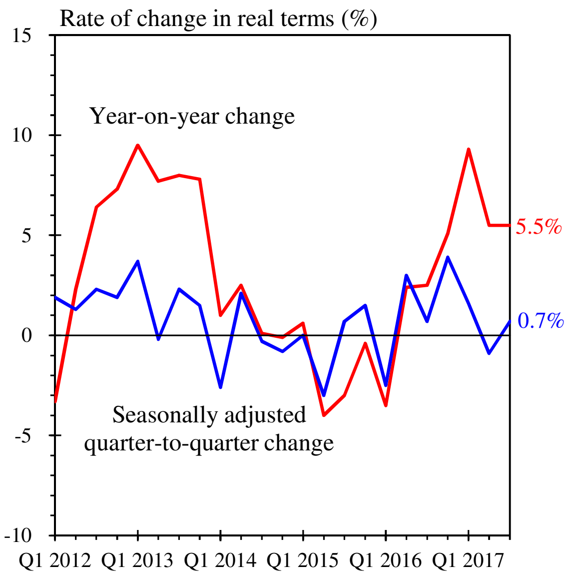
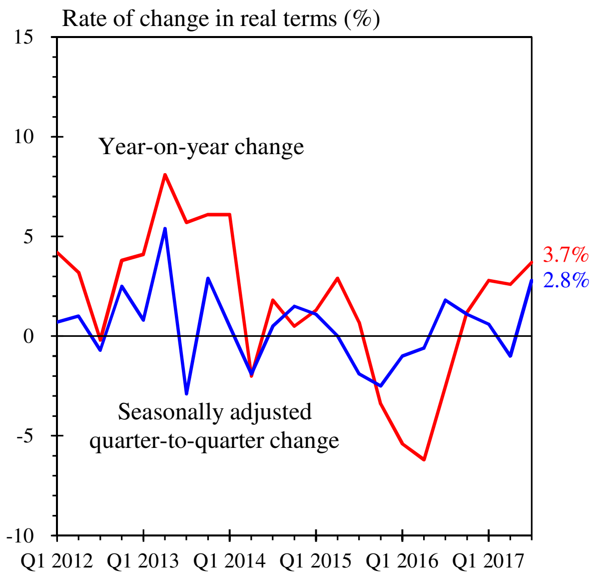


Chart 2(b) : Exports of services accelerated in growth



Domestic sector

6. Domestic demand stayed firm in the third quarter of 2017. Private consumption expenditure expanded notably by 6.7% in the third quarter of 2017, following the growth of 4.7% in the first half of the year ***(Chart 3(a))***. Local consumer sentiment continued to be underpinned by favourable job and income conditions, with additional support from a stronger boost from the positive wealth effects. Retail sales volume resumed growth in the second quarter of 2017, and the upward trend picked up in recent months, with year-on-year growth for July to October averaging 4.2%, reflecting upbeat local consumption sentiment and improvement in inbound tourism.

7. Overall investment spending in terms of gross domestic fixed capital formation recorded a modest decline of 1.7% in the third quarter of 2017, following the marked growth of 6.6% in the first half of the year ***(Chart 3(b))***. The decline in the third quarter was due partly to the decrease in machinery and equipment acquisition, a volatile component. Nevertheless, overall building and construction expenditure accelerated to show solid growth, as building and construction works in the public sector picked up markedly and those in the private sector continued to grow. For the first three quarters of 2017 combined, overall investment spending rose by 3.7%.

Chart 3(a) : Private consumption expenditure held up particularly well

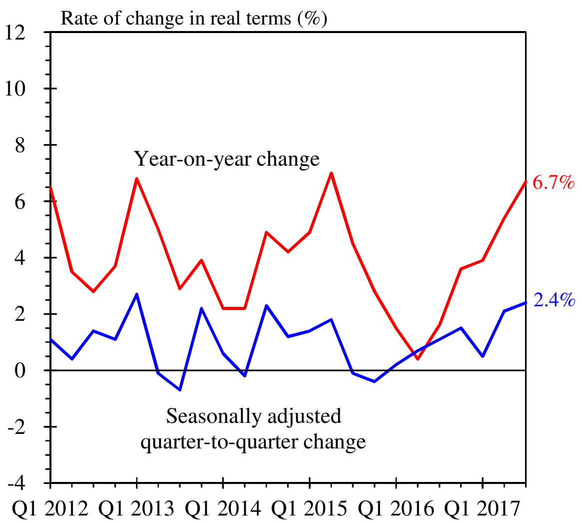
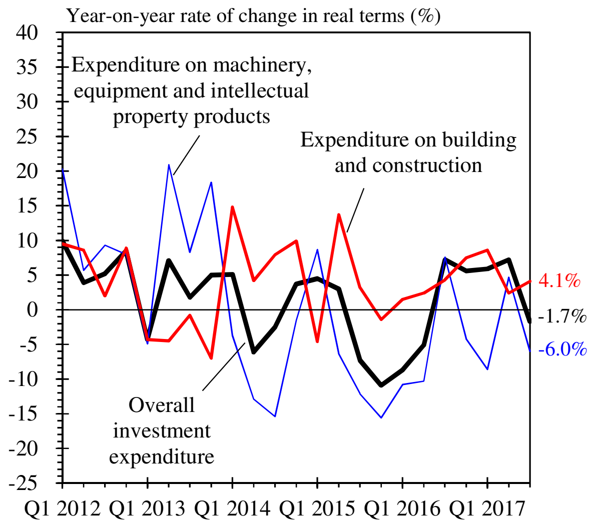


Chart 3(b) : Investment spending rose by 3.7% in real terms in the first three quarters of 2017 combined

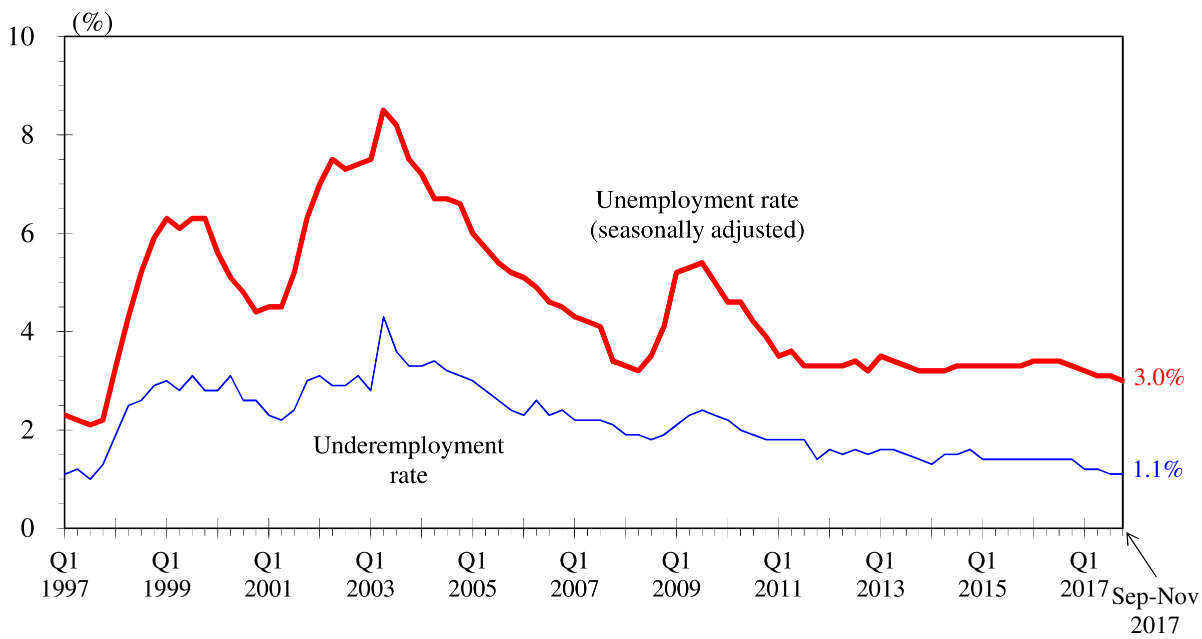


8. As for external direct investment (DI), according to breakdowns of inward DI data up to end-2016 by source, the Mainland continued to be prominent as a major source of Hong Kong's inward DI, accounting for around 26% of total position of inward DI at end-2016. Separately, the number of business operations in Hong Kong with parent companies overseas and in the Mainland climbed up to a new high of 8 225 according to the survey results for 2017. These reflect our business friendly environment as well as our prominent role as a bridge between the Mainland and the rest of the world.

Labour Market

9. The seasonally adjusted unemployment rate fell to 3.0% in September – November 2017, the lowest level in almost 20 years, while the underemployment rate also stood at a mere 1.1%, signifying a tight manpower situation ***(Chart 4)***. Growth in both labour force and total employment picked up pace, and their year-on-year increases continued to be appreciable.

Chart 4 : The labour market remained in full employment



10. The Hong Kong economy has witnessed sustained expansion since the implementation of Statutory Minimum Wage (SMW), thereby relieving to a large extent the pressure on the labour market brought about by SMW. In September – November 2017, the unemployment rates of the low paying sectors (LPS)[(2)] and non-LPS were 3.0% and 2.3% respectively, with both figures being 0.4 percentage point lower than their year-ago levels ***(Chart 5)***.

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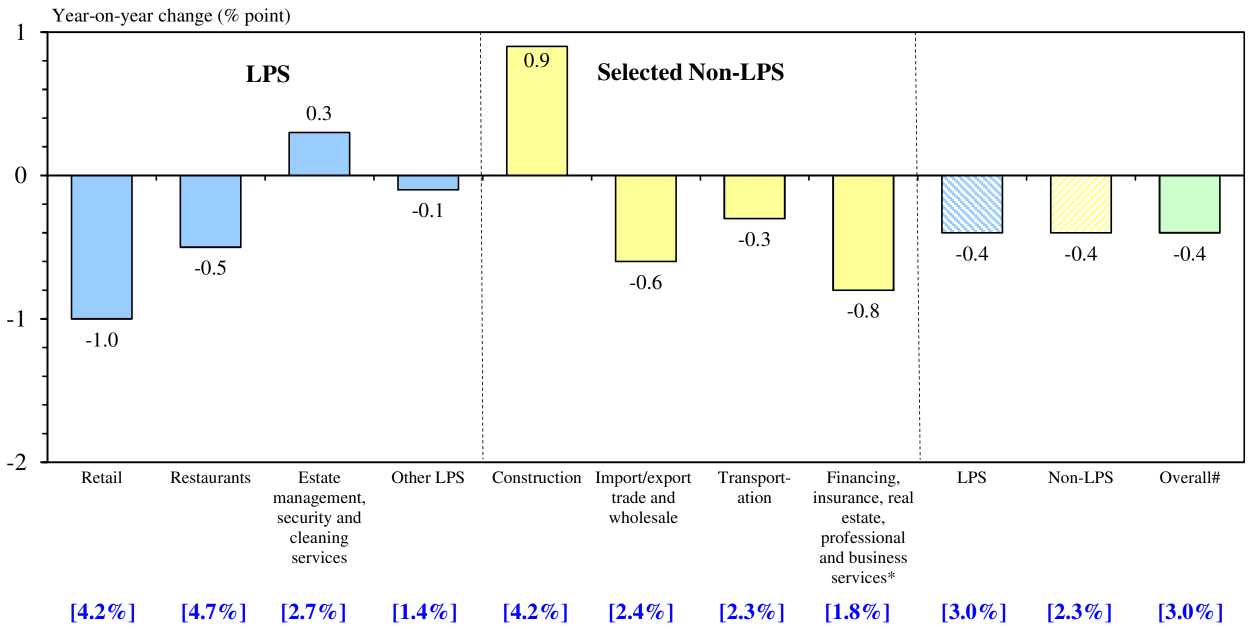
(2) The Minimum Wage Commission identified LPS as (i) retail; (ii) restaurants; (iii) estate management, security and cleaning services; and (iv) other low-paying sectors – including: elderly homes; laundry and dry cleaning services; hairdressing and other personal services; local courier services; and food processing and production.

Chart 5：Unemployment rates of most sectors declined over a year earlier



Notes: Figures in brackets refer to the unemployment rate for that sector in Sep-Nov 2017 (provisional figures).
(*) Excluding real estate maintenance management, security and cleaning services.
(#) Seasonally adjusted, and including first-time job-seekers and re-entrants into the labour force.

11. Analysed by skill segment, the unemployment rates for the higher- and lower-skilled segments in September – November 2017 fell to 1.6% and 3.2% respectively, both being 0.3 percentage point lower than their year-ago levels ***(Table 1)***.

Table 1：The employment and unemployment situations by skill segment

	Employment#					Unemployment rate#		
	Sep – Nov 2017	Change as compared to Feb – Apr 2011 (before the implementation of SMW)		Year-on-year change		Sep – Nov 2017	Change as compared to Feb – Apr 2011 (before the implementation of SMW)	Year-on-year change
	(No.)	(No.)	(%)	(No.)	(%)	(%)	(% point)	(% point)
Higher-skilled	1 514 900	+187 300	+14.1	+40 500	+2.7	1.6	-0.4	-0.3
Lower-skilled	2 325 400	+110 700	+5.0	+23 600	+1.0	3.2	-0.9	-0.3
Lower-skilled (excl. government employees and live-in domestic workers)	1 900 300	+48 300	+2.6	+3 400	+0.2			

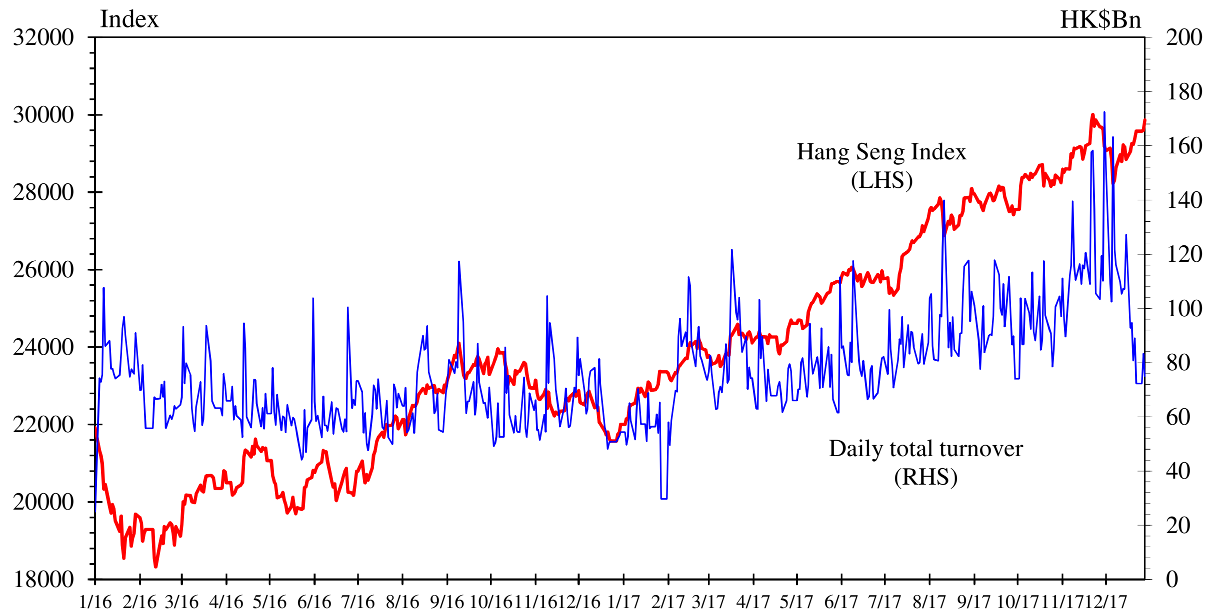
Note： (#) Provisional figures.

12. Wages and earnings registered broad-based and solid increases amid the persistently tight manpower situation. Nominal wages and payroll increased by 3.7% and 3.3% respectively in September 2017 over a year earlier, translating into real improvements of 2.2% and 1.5% respectively after discounting for inflation. The average monthly employment earnings of full-time employees of the lowest decile group (excluding foreign domestic helpers) rose by 5.4% in nominal terms, or 3.5% in real terms in August – October 2017 over a year earlier. Overall income continued to post sturdy gains as well, with the year-on-year growth of median monthly household income (excluding foreign domestic helpers) at an appreciable 5.3% in nominal terms, or 3.6% in real terms after discounting for inflation, over the same period (Please refer to ***Annex*** for details).

Asset markets

13. The local stock market rose visibly in 2017, alongside the rallies in major overseas markets, as investor sentiment remained generally upbeat upon the improved global economic outlook. The Hang Seng Index (HSI) rose to 30 003 on 22 November 2017, its highest closing level since November 2007. The HSI closed at 29 919 on 29 December 2017, up by 16.1% from end-June 2017 or 36.0% from end of 2016. Average daily turnover rose from $77.8 billion in the second quarter of 2017 to $93.2 billion in the third quarter, and further to $108.5 billion in October and November 2017 combined ***(Chart 6)***. Taking the first eleven months of 2017 together, Hong Kong ranked fourth among the major stock exchanges in the world in terms of the amount of funds raised through initial public offering.

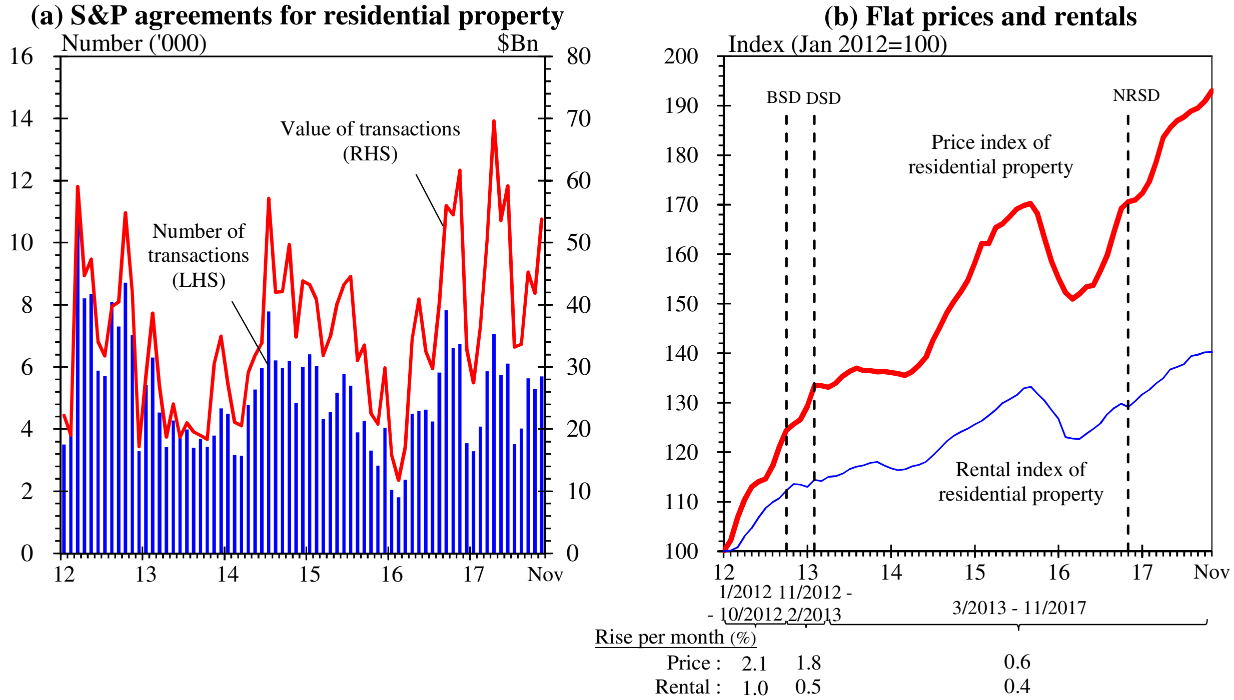
Chart 6 : Local stock market rose visibly in 2017



14. The residential property market moderated for a few months following the introduction of the eighth round of macro-prudential measures for property mortgage loans by the Hong Kong Monetary Authority (HKMA) in May 2017. Yet it showed signs of re-activation more recently. The monthly average number of sale and purchase agreements for residential property received by the Land Registry plunged by 40% from the second quarter to 3 765 in July and August. The monthly average number rose back to 5 537 during September to November ***(Chart 7(a))***.

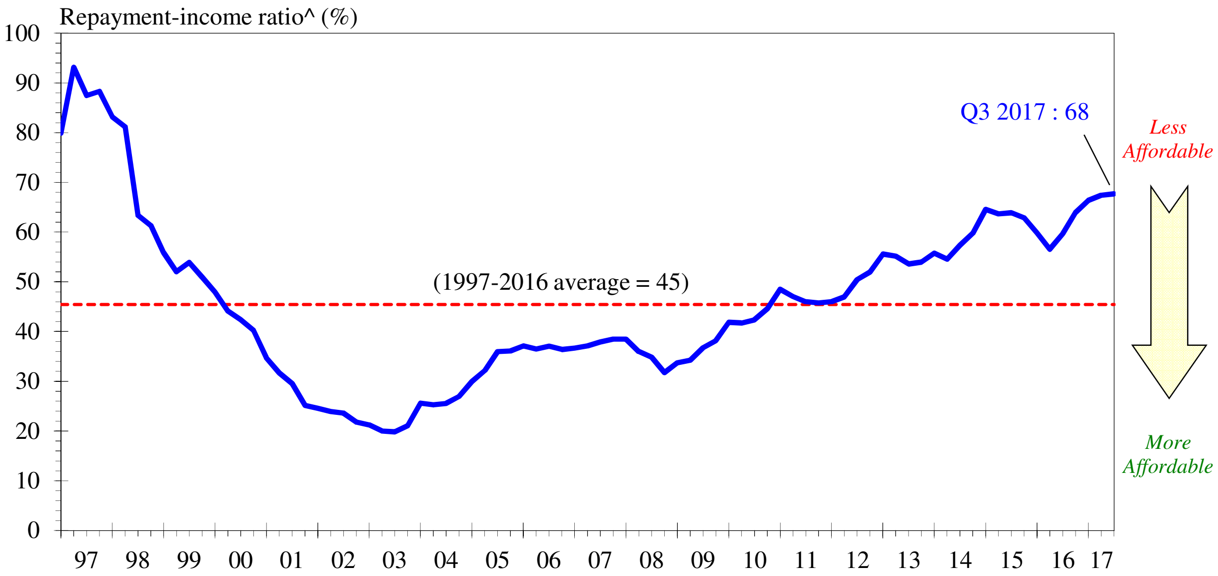
15. Overall flat prices rose at a decelerated 0.5% per month between June and September 2017, visibly lower than the hectic gain of 1.5% per month during the second quarter. Yet the rate of increase accelerated in the ensuing two months, reaching 1.1% in November. Meanwhile, overall flat rentals increased by 0.4% per month during July to November 2017, slightly slower than the increase of 0.8% per month during the second quarter ***(Chart 7(b))***.

Chart 7 : The residential property market showed signs of re-activation lately



16. As a result of the surge over the past several years, overall flat prices in November 2017 exceeded the peak in 1997 by 101%. In the third quarter of 2017, the home purchase affordability (i.e. the ratio of mortgage payment for a 45-square metre flat to median income of households, excluding those living in public housing) worsened further to around 68%, significantly higher than the long-term average of 45% over 1997-2016 ***(Chart 8)***. Should interest rates rise by three percentage points to a more normal level, the ratio would soar to 88%.

Chart 8 : The mortgage payment to income ratio worsened further



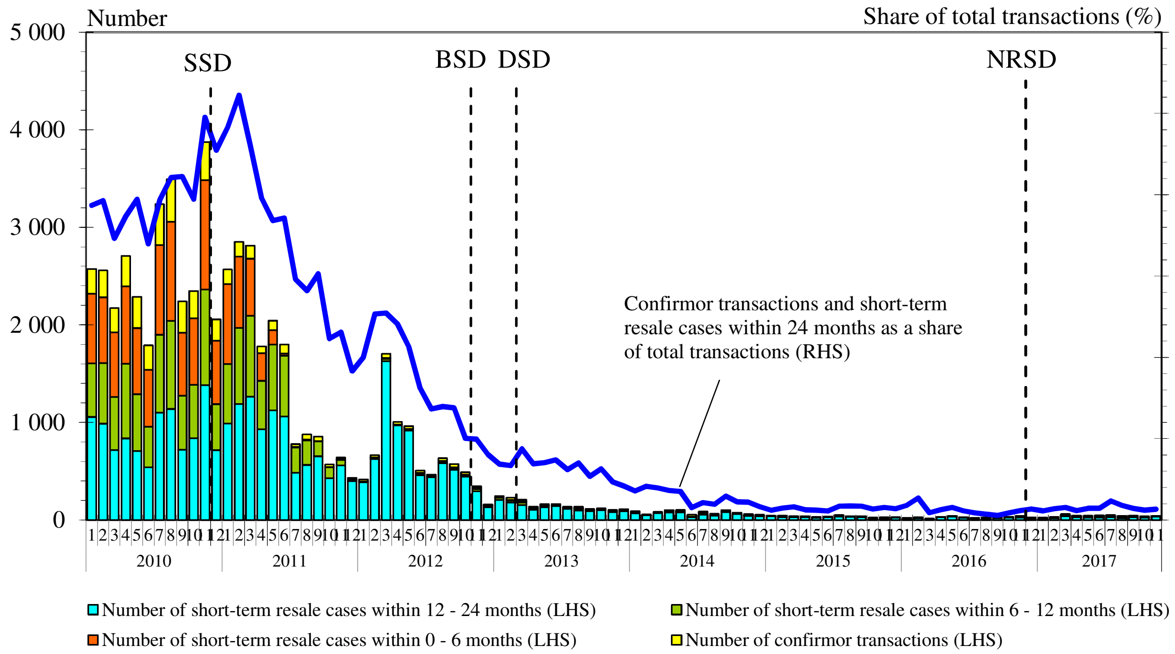
Note : (^) The ratio of mortgage payment for a flat with saleable area of 45 sq m (assuming 70% loan-to-value ratio and tenor of 20 years) to median income of households (excluding those living in public housing). This ratio is different from the debt servicing ratio published by the HKMA, which is the ratio of actual monthly debt obligations of mortgagees to their monthly income of newly approved mortgages.

17. Raising flat supply through increasing land supply is the Government's top policy priority in ensuring the healthy and stable development of the property market. As announced in December 2017, a total of 11 sites were sold or will be put up for sale in 2017-18 by the Government under the land sale program, capable of providing about 5 800 flats in total. The aggregate private housing land supply (including Government land sale, railway property development projects, the Urban Renewal Authority's projects, and private development and redevelopment projects) in 2017-18 is estimated to have a capacity to provide about 24 300 flats, exceeding the annual supply target of 18 000 flats. The total supply of flats in the coming three to four years (comprising unsold flats of completed projects, flats under construction but not yet sold and flats on disposed sites where construction can start any time) stayed at a high level of 97 000 units as estimated at end-September 2017.

18. Meanwhile, the Government has also put in efforts to reduce the possible risks to financial stability arising from an exuberant property market through managing the demand in the property market. The various demand-side management measures have yielded notable results. On speculative activities, the number of short-term resale (comprising confirmor transactions and resale within 24 months after assignment) remained low at 42 cases per month or 0.7% of total transactions in the first eleven months of 2017, well below the monthly average of 2 661 cases or 20.0% in January to November 2010 (i.e. the period before the introduction of the Special Stamp Duty) ***(Chart 9)***. Reflecting the effects of the Buyer's Stamp Duty, purchases by non-local individuals and non-local companies also stayed low at 94 cases per month or 1.6% of total transactions in the first eleven

months of 2017, much lower than the monthly average of 365 cases or 4.5% in January to October 2012 ***(Chart 10)***. As an indicator of investment activities, purchases subject to the New Residential Stamp Duty stayed at a modest level of 652 cases per month or 11.3% of total transactions in the first eleven months of 2017, sharply below the monthly average of 1 412 cases subject to Double Stamp Duty or 26.5% in January to November 2016 ***(Chart 11)***. As to mortgage lending, the average LTV ratio of new mortgages was 50% in the first ten months of 2017, likewise considerably below the average of 64% in January to October 2009 before the first round of macro-prudential measures for residential property mortgage lending was introduced by the HKMA.

Chart 9 : Short-term speculative activities stayed subdued



Note : Confirmor transactions refer to resale before assignment.

Chart 10 : Purchases by non-local buyers remained low

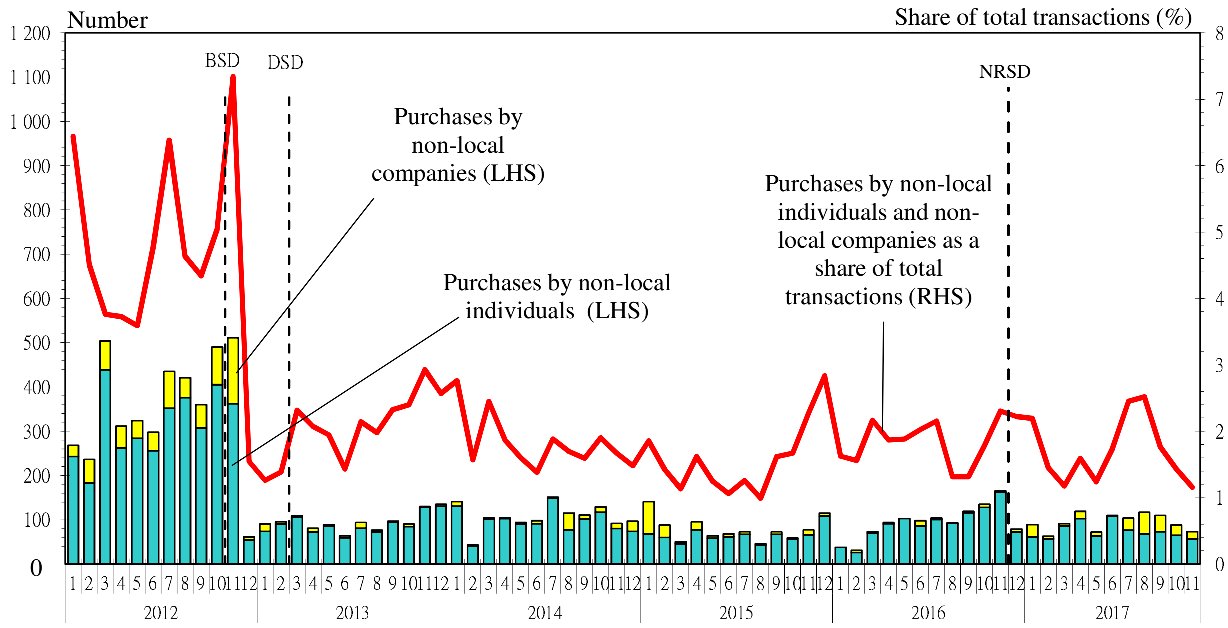
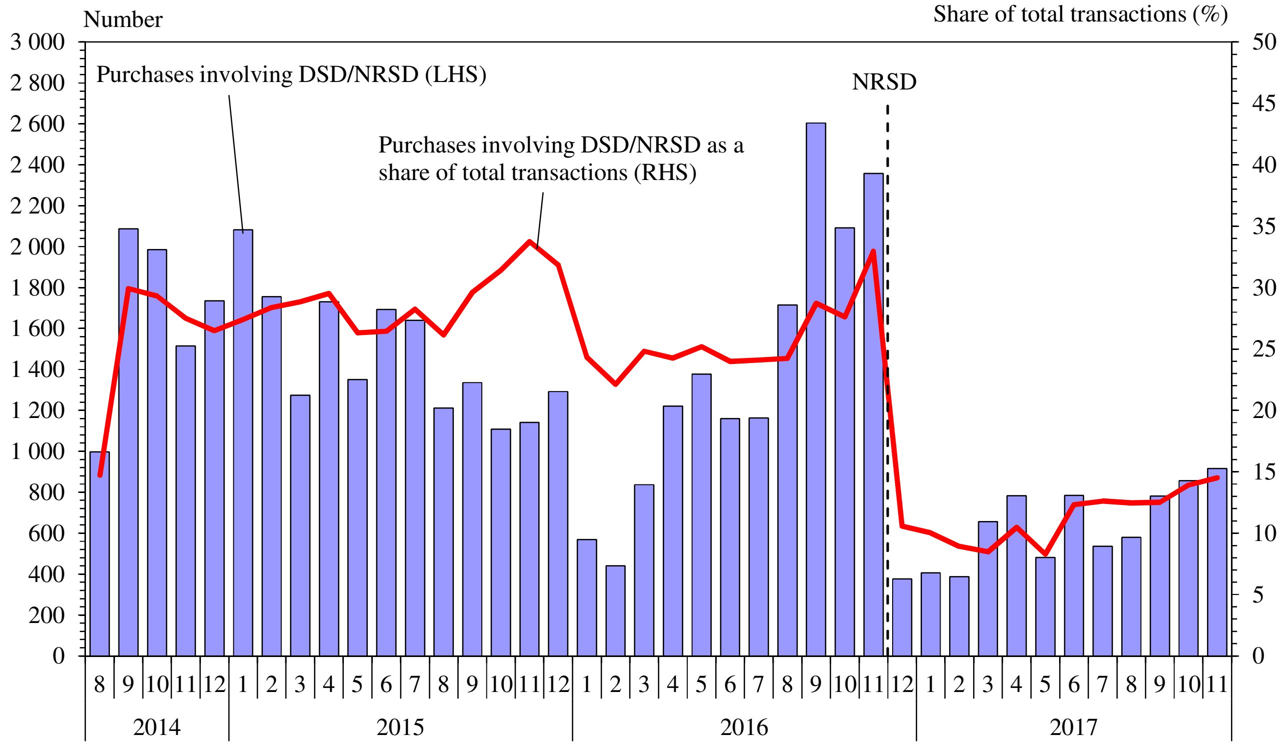


Chart 11 : Investment activities decreased visibly

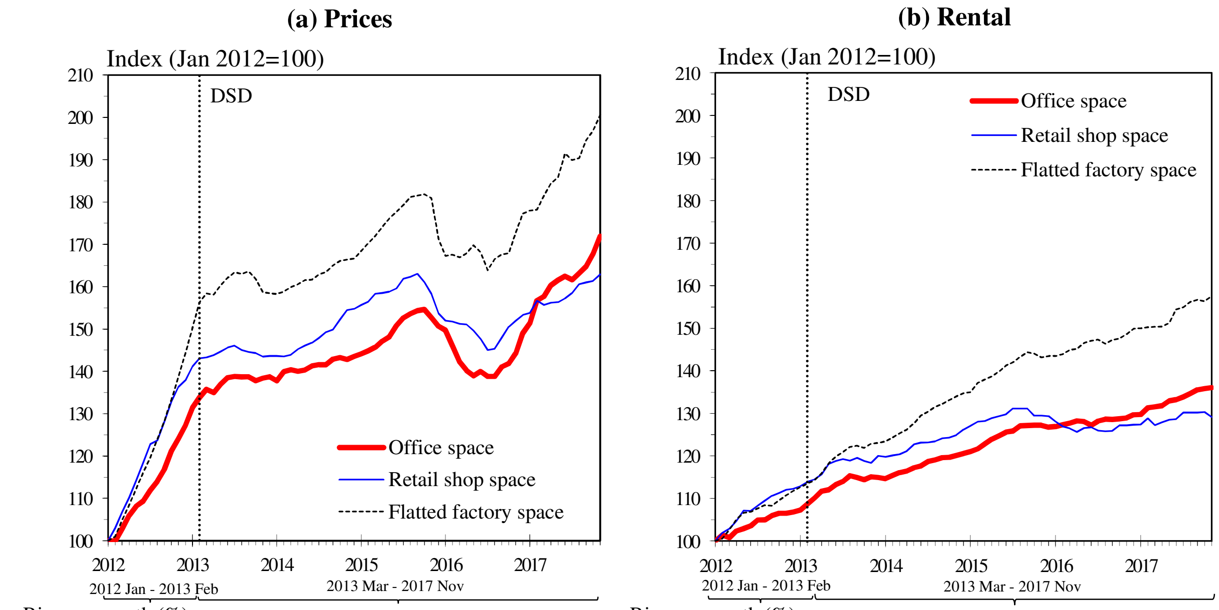


19. Looking forward, the changing fundamental factors may put pressures on the residential property market in the future. The US Fed started scaling back its balance sheet gradually in October 2017 and raised interest rates again in December. As the US interest rate normalisation process continues, local interest rates would eventually rise under the Linked Exchange Rate System. Moreover, the demand-supply balance of flats could also eventually ease when the increased

residential land supply over the past few years gradually turns into actual flat production.

20. As to the commercial and industrial property markets, prices and rentals in most market segments increased further in recent months. Overall sale prices and overall rentals of office space rose by 6% and 2% respectively between June and November 2017. For retail shop space, sale prices rose by 4% while rentals showed little change. Meanwhile, sale prices and rentals of flatted factory space rose by 5% and 2% respectively ***(Chart 12)***. Trading activities during July to November 2017 remained generally active.

Chart 12 : Prices and rentals of most non-residential properties increased further in recent months

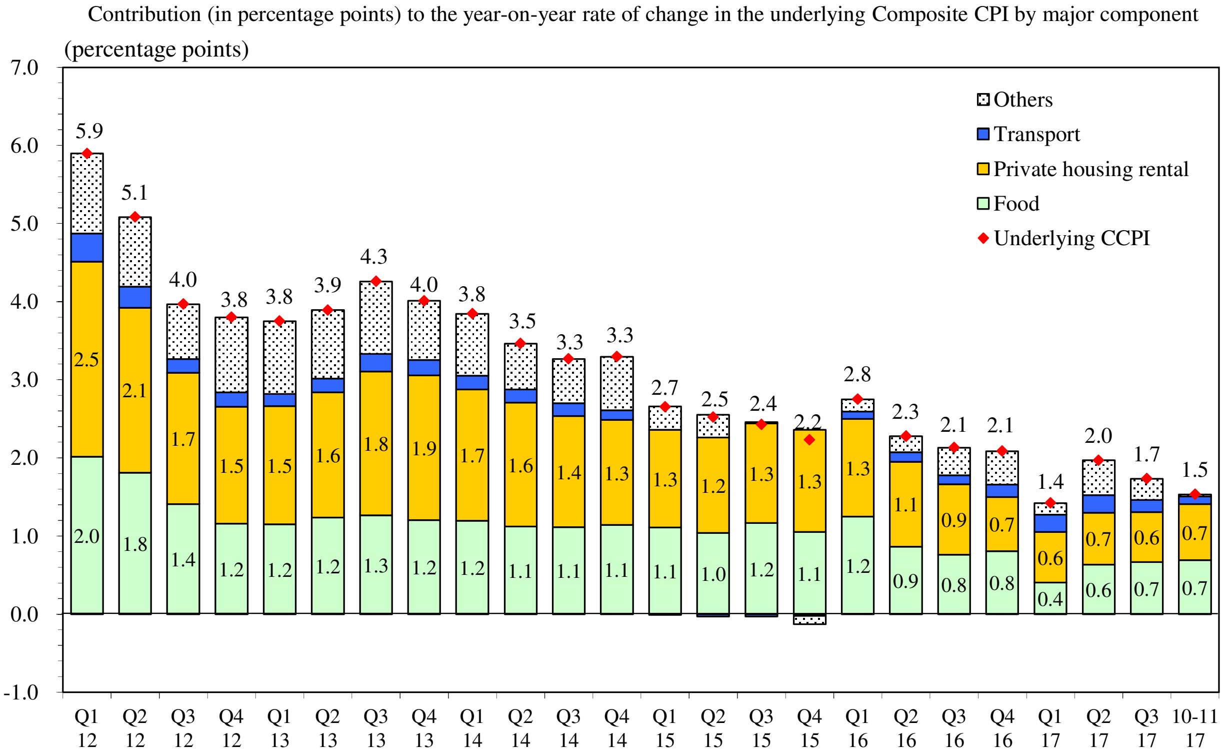


Rise per month (%)	(a) 2012 Jan - 2013 Feb	(a) 2013 Mar - 2017 Nov	(b) 2012 Jan - 2013 Feb	(b) 2013 Mar - 2017 Nov
Office space	2.0	0.4	0.7	0.4
Retail shop space	2.7	0.2	1.0	0.2
Flatted factory space	3.3	0.4	1.0	0.6

Inflation

21. Inflation pressure was largely contained, thanks to slow increases in import prices and moderate rises in local costs. Underlying consumer price inflation averaged 1.7% in the first eleven months of 2017, down from the average of 2.3% in 2016 as a whole, representing the sixth consecutive year of easing ***(Chart 13)***.

Chart 13 : Inflation eased for the sixth consecutive year



Note : The year-on-year rates of change of the underlying Composite CPIs 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.

22. Price pressures of many major components of the underlying Composite Consumer Price Index (Composite CPI) were benign ***(Table 2)***. On the two largest components by weight, food prices (including costs of dining out) rose moderately by 2.4% over a year earlier in the third quarter of 2017 and by 2.5% in October and November 2017 combined, amid modest imported food inflation. On the other hand, the year-on-year increase in private housing rent remained modest at 2.1% in the third quarter of 2017, and 2.3% in October and November 2017 combined, reflecting that the feed-through from general uptrend in fresh-letting residential rentals since the mid-2016 had only been gradual. Separately, the year-on-year increase in public housing rental component narrowed to 6.3% in the third quarter of 2017 on average, and further decelerated to 0.1% in October and November 2017 combined, as the effect from upward adjustment in public housing rentals in 2016 had dissipated since September 2017.

Table 2 : Underlying Composite Consumer Price Index by component
(year-on-year rate of change (%))

Expenditure component	Weighting (%)	2016	2016 Q1	2016 Q2	2016 Q3	2016 Q4	2017 Q1	2017 Q2	2017 Q3	2017 Oct-Nov
Food	27.29	3.4	4.6	3.2	2.8	3.0	1.5	2.3	2.4	2.5
Meals bought away from home	17.74	3.3	3.7	3.3	3.1	3.1	2.8	2.7	2.7	2.6
Other foodstuffs	9.55	3.6	6.3	3.1	2.1	2.7	-1.1	1.4	2.0	2.4
Housing[(a)]	34.29	3.3 (3.7)	4.0 (4.0)	3.5 (4.6)	3.1 (6.0)	2.8 (0.4)	2.7 (0.3)	2.7 (2.7)	2.6 (2.6)	2.4 (2.4)
Private dwellings	29.92	3.2 (3.4)	4.2 (4.2)	3.6 (4.8)	3.0 (4.1)	2.3 (0.6)	2.1 (0.5)	2.2 (2.2)	2.1 (2.1)	2.3 (2.3)
Public dwellings	1.94	3.5 (7.2)	* (*)	0.4 (0.5)	3.6 (51.3)	9.9 (-5.6)	9.9 (-5.6)	9.6 (11.5)	6.3 (7.5)	0.1 (0.4)
Electricity, gas and water	2.67	0.6 (1.0)	-1.1 (*)	-1.6 (-1.1)	4.0 (4.1)	1.4 (1.4)	-5.5 (-5.5)	-1.0 (-1.0)	-0.3 (-0.3)	* (*)
Alcoholic drinks and tobacco	0.54	1.5	0.3	1.2	2.4	2.1	2.3	1.0	-0.2	-0.7
Clothing and footwear	3.21	-3.4	-3.3	-2.8	-4.5	-3.0	-1.9	-1.4	1.0	0.2
Durable goods	4.65	-5.4	-5.7	-5.4	-5.3	-5.0	-3.6	-3.6	-3.3	-2.7
Miscellaneous goods	3.56	1.5	0.5	1.3	2.3	2.1	2.3	1.8	0.5	0.7
Transport	7.98	1.6	1.2	1.5	1.4	2.1	2.9	2.9	2.0	1.2
Miscellaneous services	15.81	2.3	2.7	2.1	2.5	1.9	0.6	2.2	0.9	-0.1
All items	100.00	2.3 (2.4)	2.8 (2.8)	2.3 (2.6)	2.1 (3.1)	2.1 (1.2)	1.4 (0.5)	2.0 (2.0)	1.7 (1.8)	1.5 (1.5)

Notes : (a) The housing component covers rents, rates, Government rent, maintenance costs and other housing charges. Its sub-components on private and public dwellings as presented here, however, cover rents, rates and Government rent only. Hence, the combined weighting of private and public dwellings is slightly less than the weighting of the entire housing component.

( ) Figures in brackets represent the headline rates of change before netting out the effect of Government's one-off relief measures.

(*) Change within ±0.05%.

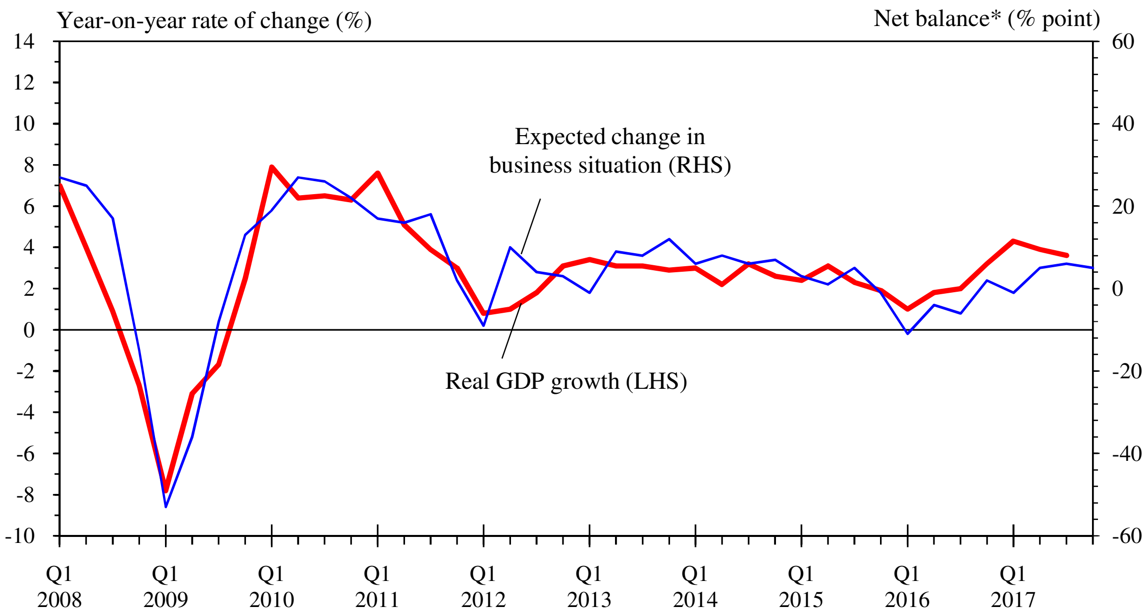
Updated economic forecasts for 2017

23. Along with an improving global outlook, major advanced economies have maintained their expansionary trend in the fourth quarter of 2017, whereas the Mainland economy has sustained its solid momentum and stable development. The expansion in global demand has boded well for Hong Kong's goods exports. Exports of services will also benefit from recovery in inbound tourism.

24. Domestic demand should hold up well, buttressed by sanguine consumption sentiment under the favourable employment and income conditions, as well as intensive building and construction activity level. Recent surveys on enterprises also continued to point to positive business sentiments ***(Chart 14)***.

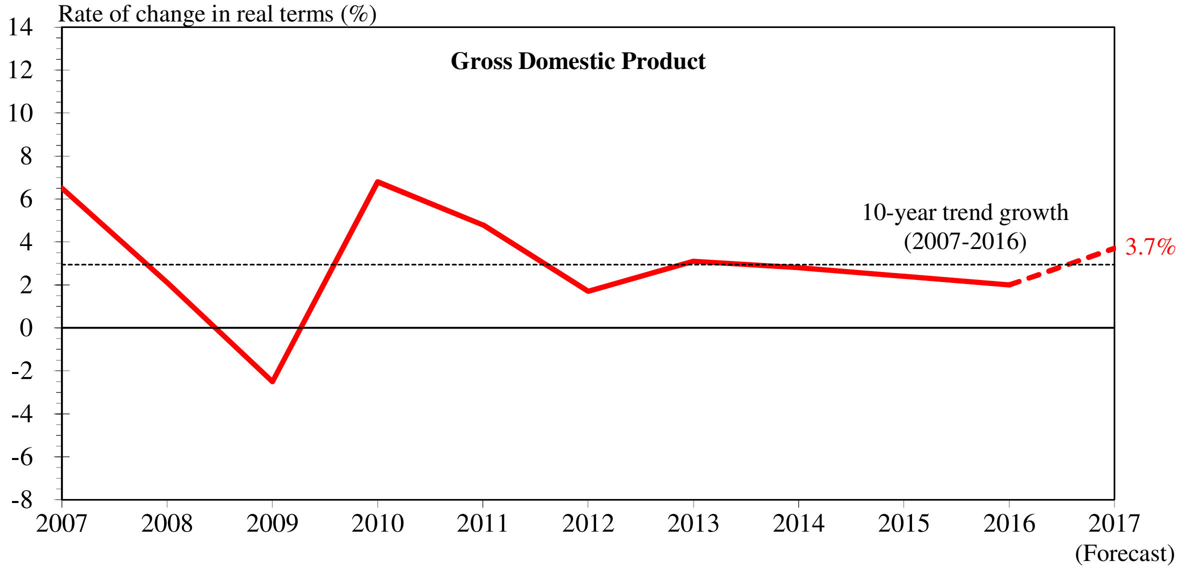
25. Taking into account the actual growth outturn of 3.9% in the first three quarters of 2017, and as the economy is expected to have grown solidly in the fourth quarter of 2017, the economic growth for 2017 as a whole is expected to reach 3.7% ***(Chart 15)***. For reference, the IMF in October 2017 projected Hong Kong's economic growth for 2017 at 3.5%, whereas the latest forecasts by private sector analysts ranged from 3.3% to 3.8%, averaging around 3.6%.

Chart 14 : Sentiments among large enterprises remained positive



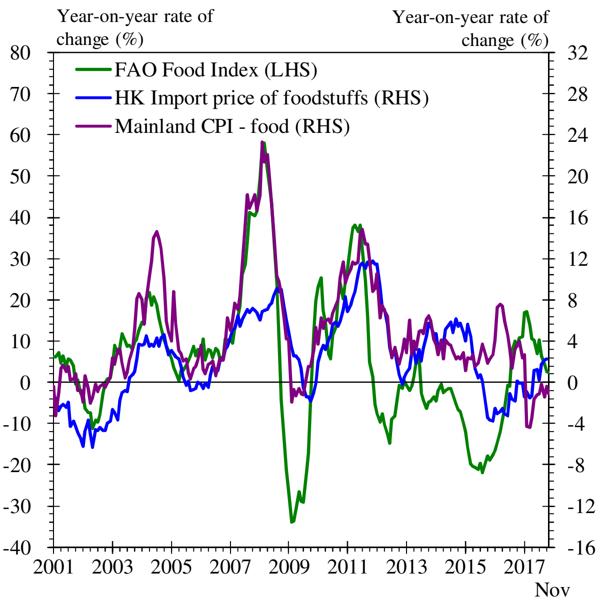
Note : (*) Net balance indicates the direction of expected change in business situation versus preceding quarter. It refers to the difference in percentage points between the proportion of establishments choosing "better" over that choosing "worse". A positive sign indicates a likely upward trend while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

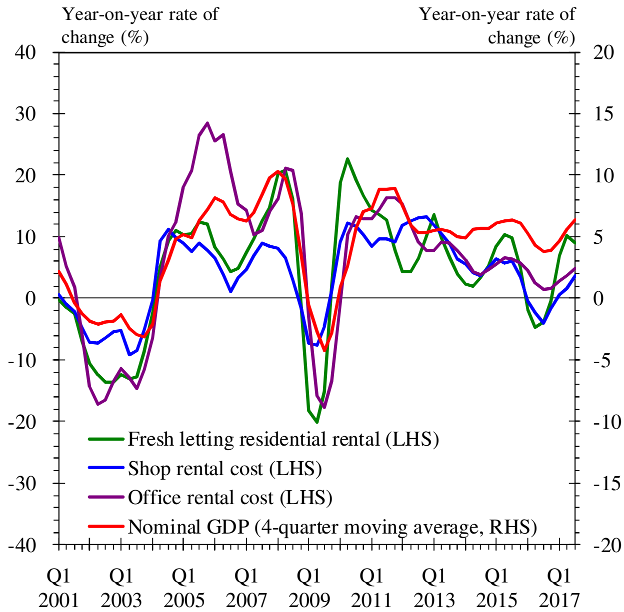
Chart 15 : Economic growth for 2017 as a whole is forecast at 3.7%



26. On inflation, the underlying and headline consumer price inflation rates for the first eleven months averaged 1.7% and 1.5% respectively, as increases in import prices and local costs remained moderate ***(Chart 16)***. The forecast rates for underlying and headline consumer price inflation for 2017 as a whole are 1.7% and 1.5% respectively, lower than those of 2.3% and 2.4% in 2016. For reference, the IMF in October 2017 forecast Hong Kong's headline consumer price inflation for 2017 at 2.0%, whereas the latest forecasts by private sector analysts ranged from 1.5% to 1.8%, averaging around 1.6%.

Chart 16 : Increases in import prices and local costs remained moderate





Economic outlook for 2018

27. The global economy is expected to maintain moderate expansion in 2018. In October 2017, the IMF forecast global economic growth at 3.7% in 2018, slightly higher than that of 3.6% in 2017. At the same time, the IMF pointed out that the global economic outlook is still subject to various uncertainties.

28. Among the advanced economies, the US economy has performed well ***(Chart 17)***. In particular, personal consumption expenditure grew solidly, whereas non-residential fixed investments and exports recovered. Along with the economic progress, unemployment rate was at 4.1% in November 2017, the lowest level in nearly 17 years. Given favourable employment situation and economic sentiment, the US economy should hopefully maintain moderate growth in 2018. However, uncertainties on the policy front still warrant attention. The US government is going to implement its tax reform package, which could possibly provide some stimulus to the US economy in the near term. Yet, its longer-term impacts, including the impacts on US fiscal deficit, future path of US monetary policy normalisation and the global fund flows, as well as whether other economies would respond with concrete policy actions, remain to be seen.

Chart 17 : The US economy has performed well, with the unemployment rate falling to a multi-year low

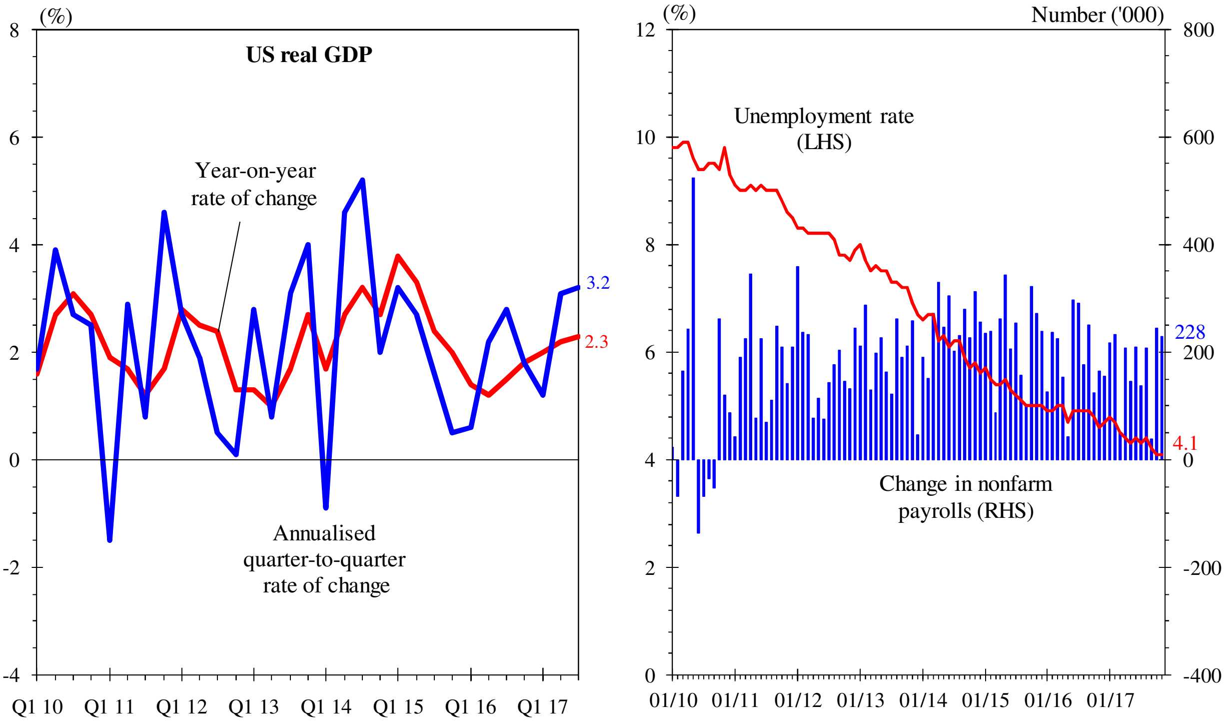
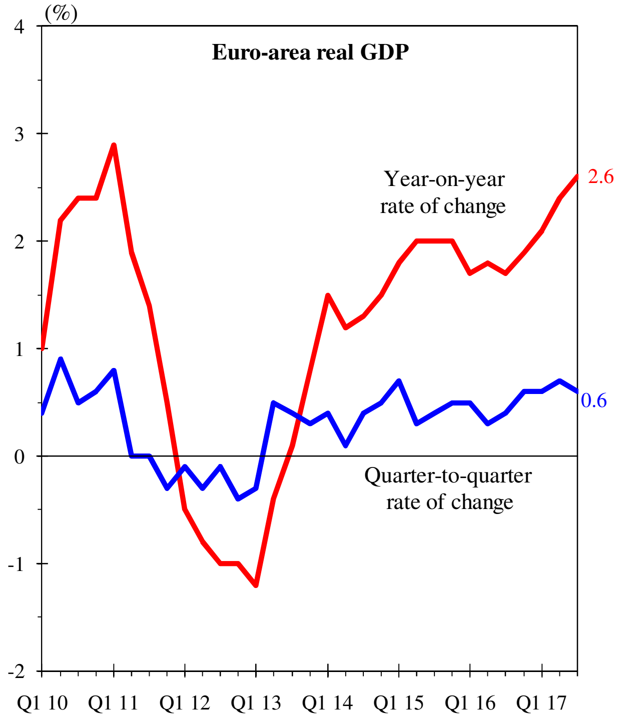
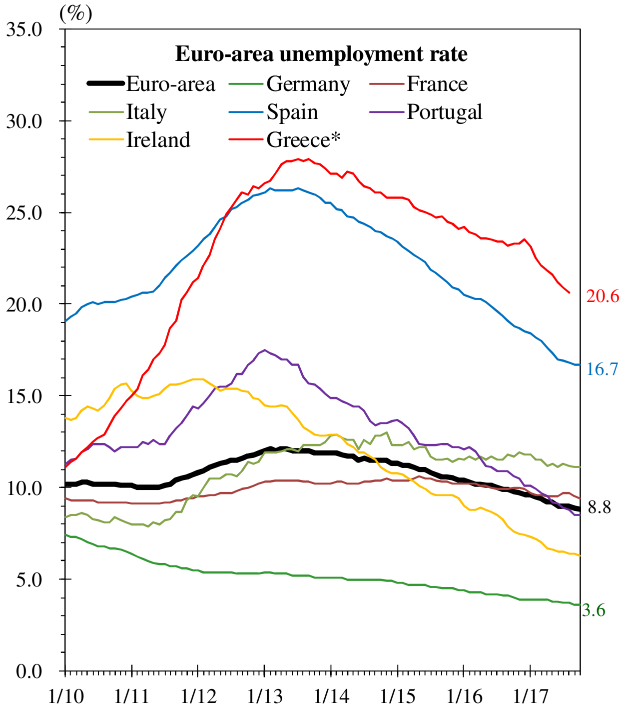


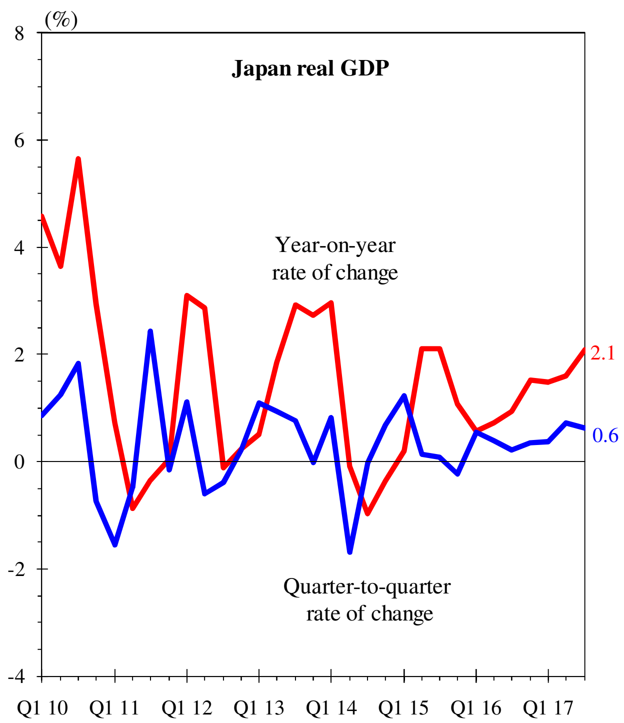
Chart 18 : The recovery in the euro-area economy has become more entrenched

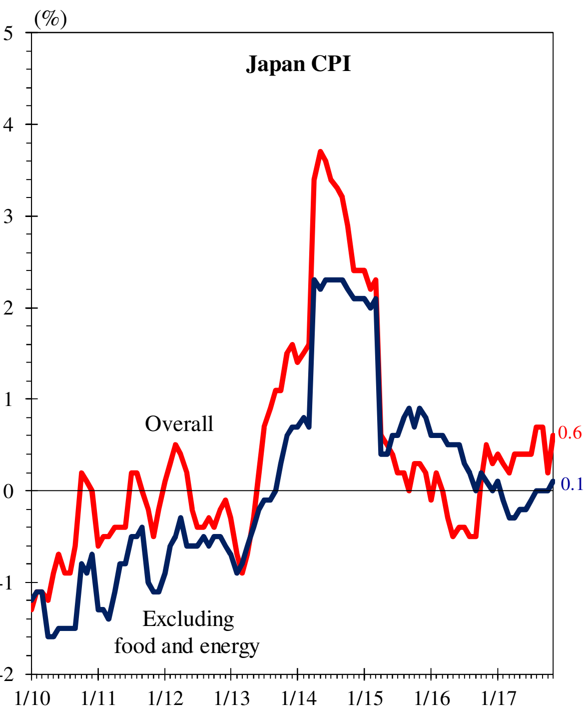




Note: (*) Latest figure available up to August 2017.

Chart 19 : Japan's economic performance improved but inflation remained low



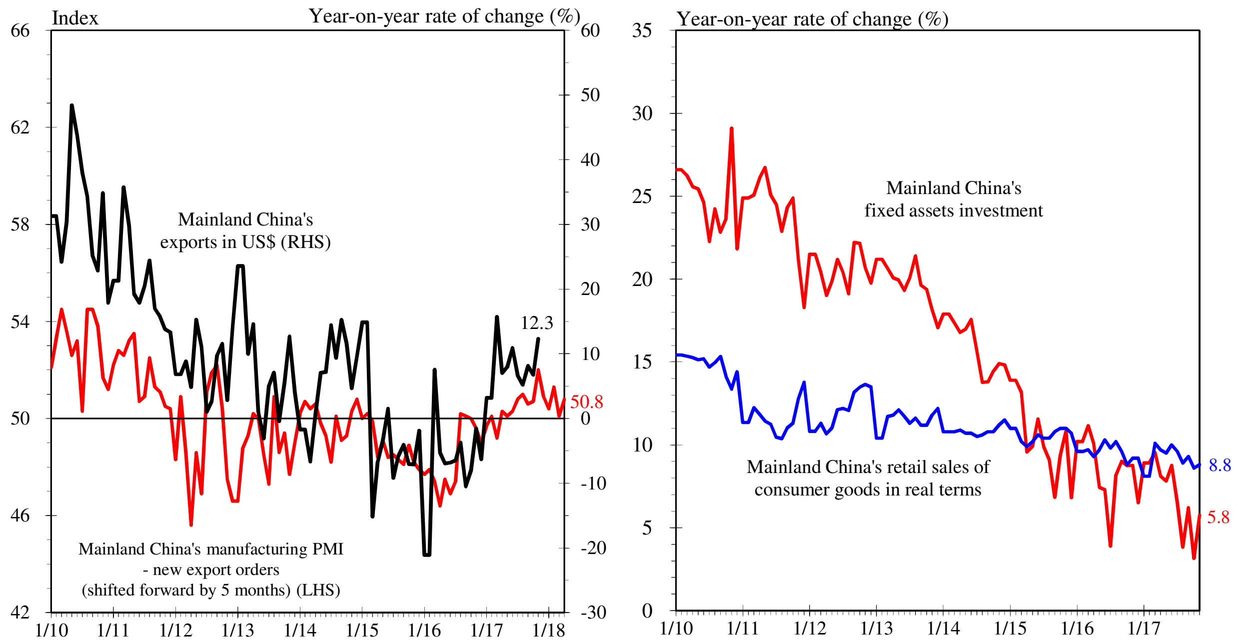


29. The recovery in the euro-area economy has become more entrenched. The economy picked up to grow by 2.6% over a year earlier in the third quarter of 2017 ***(Chart 18)***. Deflation risks have also receded in tandem. Also, those acute risks under the market radar in early 2017 which could destabilise the political situation in Europe have not materialised. These developments are all conducive to the business sentiment and investments in the euro area. Regarding the negotiations related to Brexit, the UK and the EU made sufficient progress in the first phase of the negotiations in December 2017 and will launch the second phase of the negotiations on future relationship between the two places. Yet, the market is still concerned that the trade barriers between the two sides could rise significantly after Brexit as the deadline for its negotiations in March 2019 looms. Apart from that, the political developments in Europe, including the general election in Italy in early 2018, are also closely watched by the market.

30. Japan's economy also improved recently ***(Chart 19)***, mainly driven by the strengthening of export activities. However, the recovery in Japan's economy has yet to put on a firmer footing. Its growth potential remains constrained by the structural issues such as elevated public debt and population ageing.

31. Thanks to the revival in global demand, performances of emerging Asian economies have been generally solid, with regional trading and manufacturing activities turning more vibrant in 2017. Within Asia, the Mainland economy has sustained solid momentum and stable development, with domestic demand remaining robust and exports growing visibly ***(Chart 20)***. The Mainland economy picked up somewhat to grow by 6.9% over a year earlier in the first three quarters of 2017, and should easily achieve the full-year official growth target of around 6.5% set in early 2017. Separately, as the Central Government further deepens supply-side structural reforms, steers the economy to be more service-oriented, promotes innovation and upgrading of the economy, and continues to strictly control financial risks, the Mainland economy is expected to maintain growth at medium-high speed in the period ahead.

Chart 20 : The Mainland economy maintained medium-high speed growth in the first three quarters of 2017, as domestic demand remained robust and exports grew visibly



32. On the monetary environment, as the US economy continued to improve, the Fed started scaling back its balance sheet in October 2017, and will continue to raise interest rates in a gradual manner. That said, the pace of monetary policy normalisation will still hinge on economic performance and inflation there, including the economic impacts from implementation of the tax reform. In the euro area, alongside the economic recovery there, the ECB announced to slow its pace of monthly net asset purchases starting from January 2018, to €30 billion per month. Furthermore, central banks in the UK, Canada and Korea have already raised interest rates in the second half of 2017. Even for the Bank of Japan, which adopts a greater degree of monetary policy accommodation, also indicated in the meeting at end-October 2017 that additional monetary accommodation might bring about side effects. As central banks in advanced economies could further adjust the extent of their monetary stimuli in the period ahead, global fund flows and financial markets may turn more volatile from time to time, with ensuing spillover to economic sentiment.

33. Overall, the global economy is expected to grow moderately, rendering growth impetus for exports in Asia and Hong Kong. Yet, there remain some uncertainties surrounding the external outlook, including the pace of US monetary policy normalisation, the changes in direction of monetary policies by some other major central banks, the risks of rising protectionist sentiment, as well as the heightened geopolitical tensions. These factors need to be watched over.

34. On the local front, domestic demand would be supported by factors including the prevailing optimistic economic sentiment, favourable job and income conditions as well as the ongoing infrastructure works. However, as the global monetary environment will turn more complicated in 2018, there exist risks of abrupt tightening in global liquidity conditions. Moreover, the US monetary policy normalisation will continue. As these uncertainties may affect local asset prices and economic sentiment, the Government will not be complacent about them.

35. On prices, the price trend will hinge on a host of factors, including exchange rates, international commodity prices, inflation in our major import sources and local costs. Global inflation has remained low of late, which should help ease the upward pressure on import prices. Together with the moderate rises in local costs recently, inflation pressure should remain limited in the near term. Yet, local inflation pressure will trend somewhat upwards in the period ahead as the local economy continues to expand. For reference, the headline consumer price inflation forecast for Hong Kong in 2018 by the IMF in October 2017 was 2.2%, and the latest forecasts by private sector analysts likewise averaged 2.2%.

36. The Government will closely monitor the developments on the domestic and external fronts, take into account the relevant factors, and announce the economic growth forecast for 2018 along with the 2018-19 Budget in February 2018. For reference, the IMF in October 2017 forecast economic growth for Hong Kong in 2018 to be 2.7%, while the latest forecasts from private sector analysts were mostly in the range of 2.5-3.5%.

Economic Analysis and Business Facilitation Unit
Financial Secretary's Office
29 December 2017

Annex

Recent situation of household income[1]

Background

This Annex provides a regular update on the latest trends of household income and employment earnings among various groups. As the level of Statutory Minimum Wage (SMW) has been raised from $32.5 per hour to $34.5 per hour since May 2017, the benchmark of monthly household income for low-income households is also increased from $7,600 to $8,100 (at constant Q2 2017 prices), adjusted by inflation[2], so as to reflect the latest circumstance.

Overall situation of household income and employment earnings

2. The labour market has remained tight in 2017. On a year-on-year comparison, total employment in September – November 2017 increased by 1.7%, while the seasonally adjusted unemployment rate fell to 3.0%, a low level last seen in early 1998. Median household income, a reflection of the overall income, registered appreciable growth in the third quarter of 2017, by 4.9% year-on-year in nominal terms or 3.1% in real terms after adjusting for inflation.

3. On the back of the favorable economic performance and robust labour demand, overall wages and earnings registered broad-based and solid increases. The average employment earnings of full-time employees of the lowest decile group grew by 6.8% year-on-year in the third quarter of 2017. After netting out inflation, there was a real improvement of 4.6%. Wages of the lower-skilled workers also increased by 3.7% in nominal terms and 2.2% in real terms in September 2017. For higher-skilled staff, the Salary Index for Managerial and Professional Employees indicates that employees in the same company and occupation enjoyed nominal and real year-on-year salaries growth of 4.9% and 3.1% respectively in June 2017 ***(Table 1)***.

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(1) Foreign domestic helpers are excluded from the analysis except general labour market statistics.

(2) Being adjusted based on Consumer Price Index (A).

Table 1 : Selected household income / employment earnings indicators (year-on-year rate of change (%))

Period		Median monthly household income		Wages		Employment earnings in the lowest decile^		Salaries of managerial and professional employees~	
2014		4.5	(0.1)	4.2	(-2.4)	4.6	(-0.9)	5.3	(1.8)
2015		6.5	(3.4)	4.4	(0.6)	5.6	(1.5)	5.7	(3.8)
2016		2.0	(-0.4)	3.7	(1.2)	4.7	(1.9)	5.2	(2.9)
2017	Q1	4.0	(3.4)	3.6	(3.5)	3.2	(3.1)		
	Q2	4.0	(2.0)	3.8	(1.5)	6.8	(4.4)	4.9	(3.1)
	Q3	4.9	(3.1)	3.7	(2.2)	6.8	(4.6)		

Notes: (^) Average employment earnings of full-time employees.
(~) The index is released annually for June.
( ) Rate of change (%) in real terms. Since the changes in real terms are compiled by taking the corresponding headline consumer price indices as price deflators, which could be affected by Government's one-off relief measures. As such, these figures should be interpreted with caution.

Economically active households with monthly household income below $8,100 in real terms

4. In the third quarter of 2017, the number of economically active households with monthly household income below $8,100 in real terms (referred to as "low-income households" thereafter) amounted to 70 500. The corresponding proportion in total domestic households was 2.8%(3).

5. Analysing the number and proportion of low-income households over the past ten years or so suggests that their changes largely followed economic vicissitudes. During 2000 and 2008, when the economy performed persistently well for most of the period, the proportion of low-income households fell successively from a peak of 5.0% in the third quarter of 2003 to 3.4% in 2008 over the same period. After the outbreak of the global financial tsunami in late 2008, the corresponding proportion rose back to 4.0% in the third quarter of 2009 as the Hong Kong economy was mired into recession. But with economic recovery taking hold afterwards, the figure also fell back. At 2.8% in the third quarter of 2017, which was higher than a year ago (by 0.3 percentage point), such proportion was still at a relatively low level over the past ten years ***(Table 2 and Chart 1)***.

(3) All figures pertaining to low-income households in the third quarter of 2017 are provisional figures.

Table 2 : Number and proportion of low-income households*

Period	Household type: Elderly households#	Household type: Non-elderly households	**Total**	Of which: Economically active persons therein
Q3 2003	3 000	103 900	**106 900**	128 100
	(0.1)	(4.9)	**(5.0)**	[3.9]
Q3 2008	2 600	76 300	**78 800**	88 200
	(0.1)	(3.3)	**(3.4)**	[2.6]
Q3 2009	1 700	89 500	**91 200**	104 900
	(0.1)	(3.9)	**(4.0)**	[3.0]
Q3 2010	1 600	70 800	**72 400**	81 700
	(0.1)	(3.0)	**(3.1)**	[2.4]
Q3 2011	3 500	54 400	**57 900**	64 500
	(0.1)	(2.3)	**(2.4)**	[1.9]
Q3 2012	4 000	63 500	**67 500**	73 400
	(0.2)	(2.7)	**(2.8)**	[2.1]
Q3 2013	4 300	66 900	**71 200**	78 300
	(0.2)	(2.8)	**(2.9)**	[2.2]
Q3 2014	6 200	60 400	**66 600**	72 400
	(0.3)	(2.5)	**(2.7)**	[2.0]
Q3 2015	3 800	54 000	**57 700**	64 600
	(0.2)	(2.2)	**(2.3)**	[1.8]
Q3 2016	6 700	56 100	**62 800**	68 900
	(0.3)	(2.2)	**(2.5)**	[1.9]
Q3 2017	6 700	63 800	**70 500**	77 800
	(0.3)	(2.5)	**(2.8)**	[2.1]

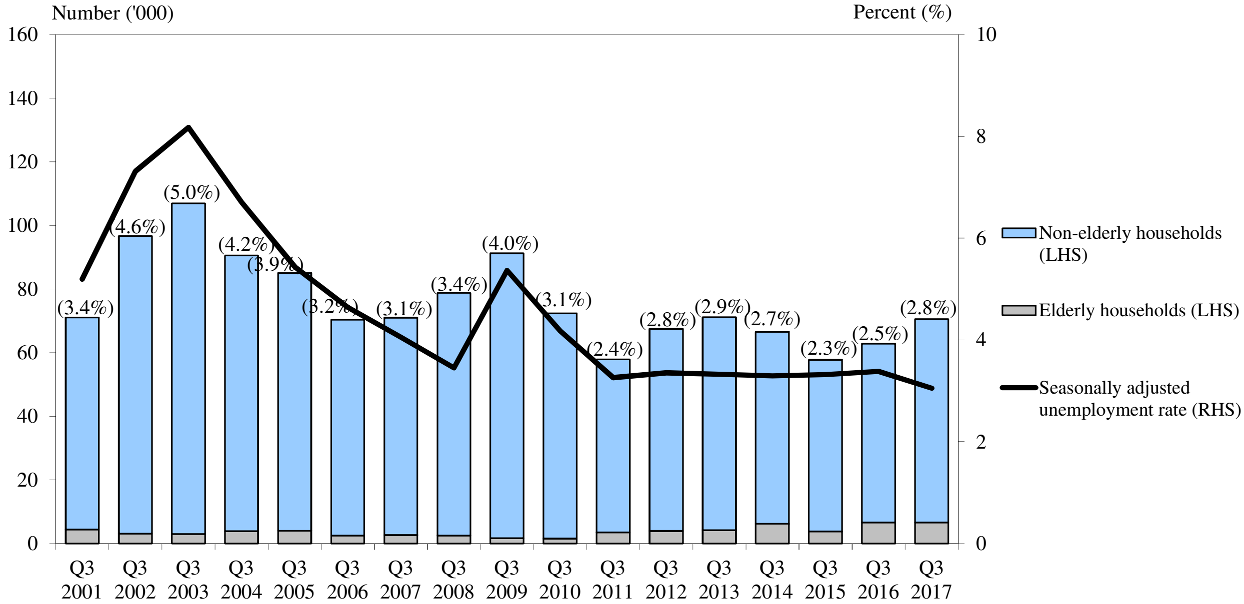
Notes :
(*) Low-income households refer to households with monthly household income less than $8,100 at constant Q2 2017 prices. This does not include households with all members being economically inactive.

(#) Elderly households refer to domestic households with all members aged 65 and above.

( ) Proportion in all domestic households (%).

[ ] Proportion in total labour force (%).

Chart 1 : Number of low-income households*



Notes : (*) Low-income households refer to households with monthly household income less than $8,100 at constant Q2 2017 prices. This does not include households with all members being economically inactive.
Figures in brackets are the proportions of low-income households in all domestic households.

Socio-economic characteristics of low-income households

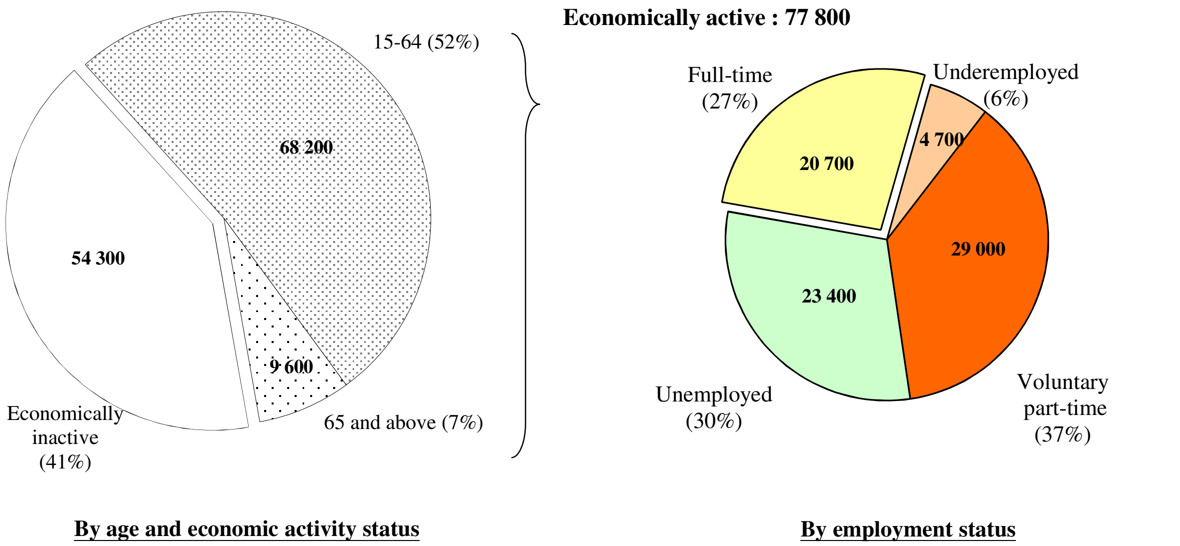
6. Further decomposition of low-income households in the third quarter of 2017 reveals the following observations:

- 132 100 persons were residing in the households in question, among whom 77 800 were economically active. Most of these individuals (68 200 or 88%) were persons aged 15-64, with the majority within the age group of 40-64 (50 400 or 65%), whilst those aged 65 and above amounted to 9 600 (12%).

- The remaining 54 300 persons were economically inactive. 25 200 of them (46%) were either children aged below 15 or elderly persons aged 65 and above.

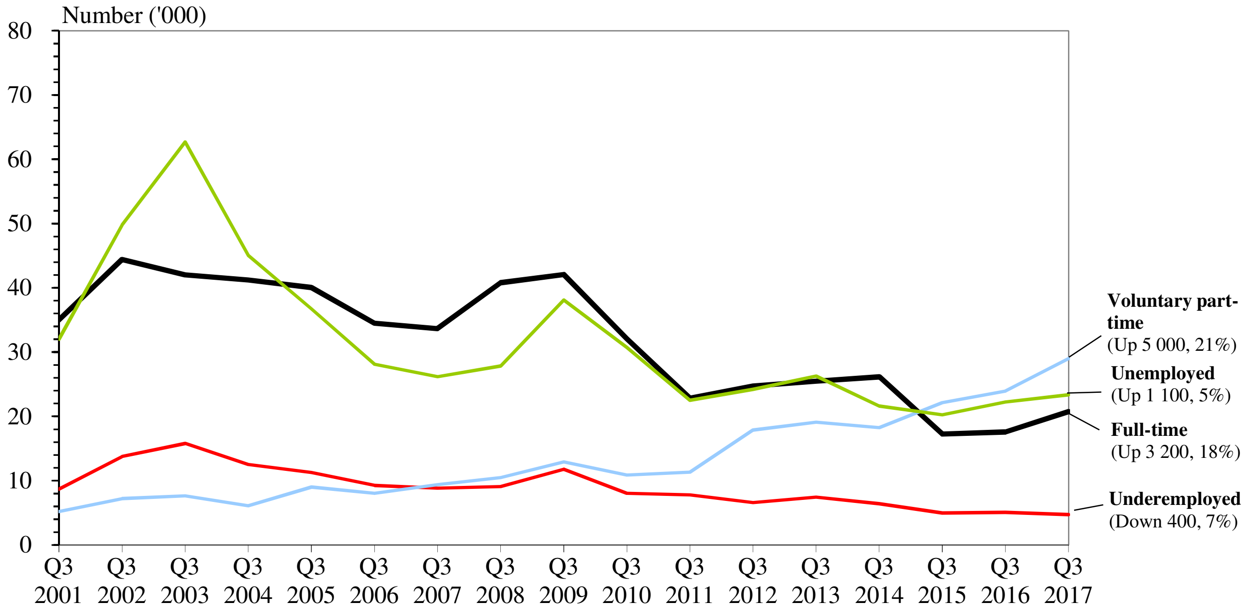
- A more in-depth analysis by employment status shows that among these 77 800 economically active persons, 27% were full-time workers, while the respective proportions for voluntary part-timers, unemployed and underemployed were 37%, 30% and 6% ***(Chart 2)***. Among these, the number of full-time workers and voluntary part-timers rose markedly by 18% and 21% respectively over a year ago ***(Chart 3)***.

Chart 2 : Persons living in low-income households* by age and economic activity status, Q3 2017



Note : (*) Low-income households refer to households with monthly household income less than $8,100 at constant Q2 2017 prices. This does not include households with all members being economically inactive.

Chart 3 : Composition of economically active persons in low-income households*



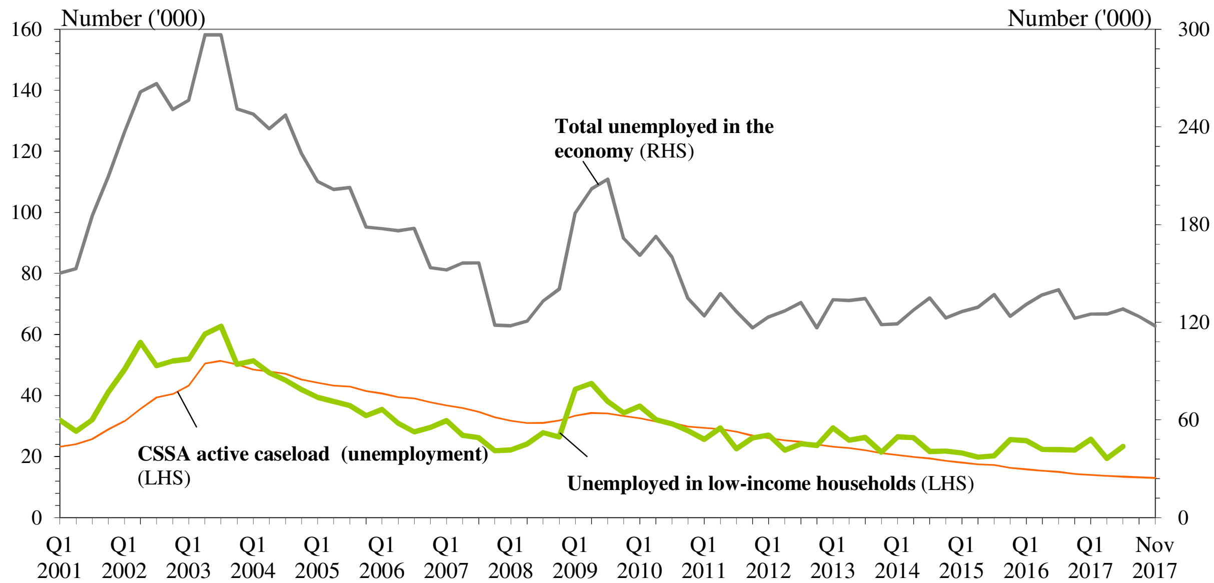
Notes : (*) Low-income households refer to households with monthly household income less than $8,100 at constant Q2 2017 prices. This does not include households with all members being economically inactive.
Figures in brackets are the year-on-year changes in number of economically active persons in Q3 2017.

- Analysed by occupation, the majority of the employed persons living in low-income households (83%) were lower-skilled workers (among whom 37% were elementary workers, and 28% were service and sales workers). A breakdown by economic sector reveals that most of them were engaged in the retail, accommodation and food services sector (16 100 or 30%), followed by transportation (5 300 or 10%).

The number of CSSA cases

7. The lower-skilled unemployment rate in September – November 2017 fell by 0.3 percentage point on a year-on-year comparison to 3.2%. Meanwhile, the number of overall CSSA caseload declined by 4 812 (or 2.0%) to 232 846 in November 2017 as compared to a year earlier. The decrease in unemployment cases was even more distinct, down by 1 470 (or 10.2%) to 12 978 over the same period ***(Chart 4)***, decreasing for 99 consecutive months. This indicates a manifestation of the self-reliance of grassroots workers who were able to leave the social security net amid tight labour market conditions over the past year.

Chart 4 : The relationship between the unemployed in low-income households*, CSSA active caseload (unemployment)^, and total unemployment in the economy



Notes : (*) Low-income households refer to households with monthly household income less than $8,100 at constant Q2 2017 prices. This does not include households with all members being economically inactive.

(^) Monthly period-end figures.

Concluding remarks

8. Employment is the best route out of poverty. The Government will continue to strengthen employment / training and retraining services so as to provide support to job-seekers, and assist needy persons who cannot provide for themselves through the social security system on a reasonable and sustainable basis. The Government will also keep on investing substantially in education in order to improve the competitiveness and skills of the workforce, increase social mobility, and reduce the child poverty risk and inter-generational poverty. To improve the livelihood of the grassroots, the fundamental solution is to promote overall economic growth so as to provide more employment and income opportunities.

9. On the back of the buoyant economic performance and robust labour demand, increases in earnings have been generally observed for citizens from different segments. The Government has implemented the "Low-income Working Family Allowance" (LIFA) Scheme in 2016, which aims at relieving the financial burden of low-income working families. The Chief Executive's 2017 Policy Address released in October 2017 announced a series of improvement measures to the Scheme so as to benefit more working households. The LIFA Scheme will also be renamed as the Working Family Allowance Scheme. The Government plans to implement the relevant measures on 1 April 2018.

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