



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

The Government released the Third Quarter Economic Report 2019 on 15 November. The Economic Report, together with the press release containing the updated economic forecasts for the whole year of 2019, have been furnished to LegCo Members.

This paper analyses Hong Kong's overall economic development in the most recent period and near-term outlook, and provides some preliminary analysis on the economic prospects for 2020.

Office of the Government Economist
Financial Secretary's Office
25 November 2019

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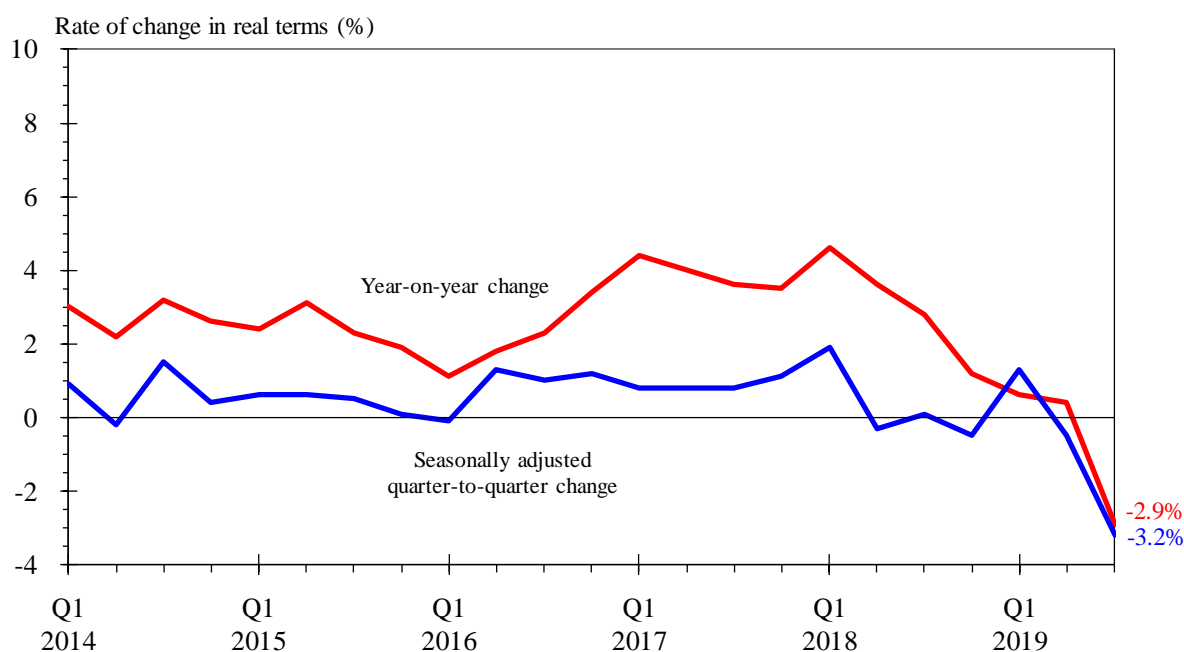
Introduction

This paper analyses the latest development of the Hong Kong economy and provides some preliminary analysis on the outlook for 2020.

Recent economic situation

2. The Hong Kong economy contracted by 2.9% ⁽¹⁾ year-on-year in the third quarter of 2019, representing an abrupt deterioration from its mild growth of 0.5% in the first half of the year. The local social incidents took a heavy toll on the consumption- and tourism-related sectors, dealing a very severe blow to an economy already weakened by a synchronised global economic slowdown and escalated US-Mainland trade tensions. External demand registered an enlarged decline in the third quarter, while domestic demand also worsened significantly. On a seasonally adjusted quarter-to-quarter comparison, real GDP contracted significantly by 3.2% in the third quarter, having shrunk by 0.5% in the preceding quarter (*Chart 1*), indicating that the economy has entered a recession for the first time since 2009. In the first three quarters of 2019 combined, the economy contracted by 0.6% from a year earlier.

Chart 1 : The Hong Kong economy contracted in the third quarter of 2019 on both year-on-year and quarter-to-quarter comparisons



(1) Unless otherwise specified, all figures on changes in the recent economic situation, external trade and domestic sector sections of this paper are year-on-year changes in real terms.

External trade

3. The external environment turned even more austere in the third quarter of 2019. US economic growth slackened further, and the economy of the euro area stayed weak. The Mainland economy, though remaining largely resilient, also showed further deceleration. US-Mainland trade tensions escalated in August, adding further strains to the already weak global economy. The Brexit process achieved little progress, while geopolitical tensions in the Middle East intensified. These various uncertainties have led to gyrations in the global financial markets. In mid-October the International Monetary Fund (IMF) lowered its global economic growth forecast for 2019 to 3.0% (as compared to 3.2% in July), the fifth downward revision and marking the slowest growth pace in a decade.

4. Hong Kong's total exports of goods registered an enlarged decline of 7.1% in the third quarter of 2019 amid further slackening of manufacturing and trading activities worldwide (*Chart 2(a)*). Exports of goods to the US saw a further noticeable decline in the third quarter, due to moderating import demand in this market and also the expanded scope of the US' additional tariffs on the Mainland's products starting in September. Meanwhile, dragged down by the faltering economic performance of major European economies, exports of goods to the EU worsened sharply to record a double-digit decline. Exports of goods to many Asian markets, including the Mainland and Japan, also registered declines of varying degrees.

5. Hong Kong's exports of services deteriorated sharply, falling by 13.8% in the third quarter, the biggest fall since the second quarter of 2003 (*Chart 2(b)*). The local social incidents with increasing violence dealt a severe blow to inbound tourism and led to a plunge of 32.2% in exports of travel services. The fall in exports of transport services also widened visibly, reflecting subdued cargo and passenger flows. Exports of financial services as well as business and other services also fell due to weaker cross-border financial and commercial activities amid softening global economic growth.

Chart 2(a) : Total exports of goods registered an enlarged decline

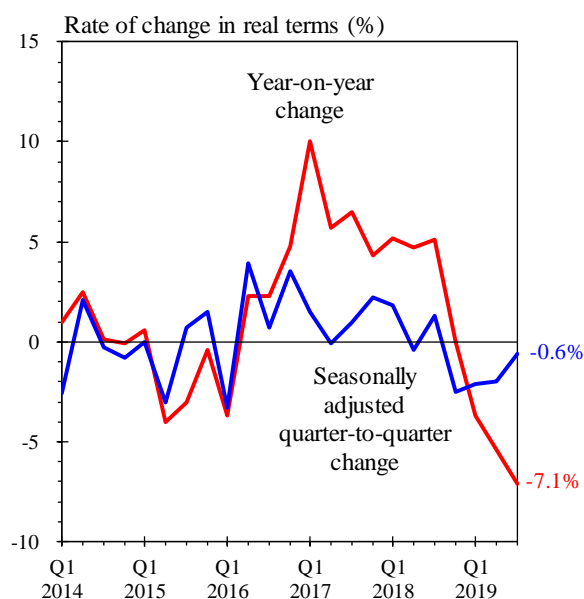
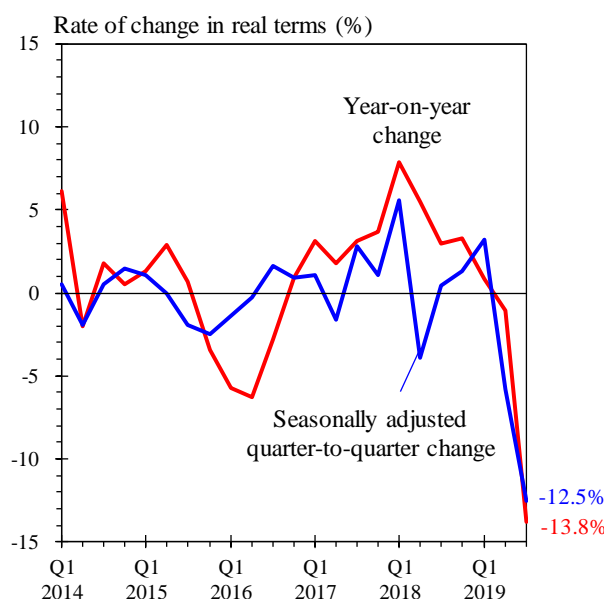


Chart 2(b) : Exports of services deteriorated sharply



Domestic sector

6. Domestic demand worsened significantly in the third quarter. Private consumption expenditure weakened sharply, falling by 3.4% and marking its first year-on-year decline since the first quarter of 2009, after expanding modestly by 1.3% in the preceding quarter (*Chart 3(a)*). The decline in private consumption expenditure was mainly attributable to the serious disruptions to consumption-related activities caused by the local social incidents and violent acts, while consumer sentiment was also dampened by the subdued economic outlook. The volume of retail sales fell sharply by 19.5% in the third quarter, almost on par with the record decline in the third quarter of 1998. Total restaurant receipts deteriorated sharply and fell by 13.6% year-on-year in real terms in the third quarter, the largest decline since the SARS outbreak in the second quarter of 2003.

7. Overall investment spending in terms of gross domestic fixed capital formation fell by 16.3% in the third quarter, representing a further widening from its 10.8% decline in the preceding quarter (*Chart 3(b)*). Mounting external headwinds and the local social incidents inflicted considerable uncertainties on near-term business prospects. Amid very pessimistic business sentiment, expenditure on acquisitions of machinery, equipment and intellectual property products plunged by 26.6%. Meanwhile, expenditure on building and construction continued to decline by 5.7%. In addition to slower private sector building activity, spending by the public sector also shrank as the implementation of new project items was affected by the delay in the LegCo's approval of funding proposals, and new projects had yet to generate sufficient output to offset the completion of some major infrastructure

projects.

Chart 3(a) : Private consumption expenditure weakened sharply

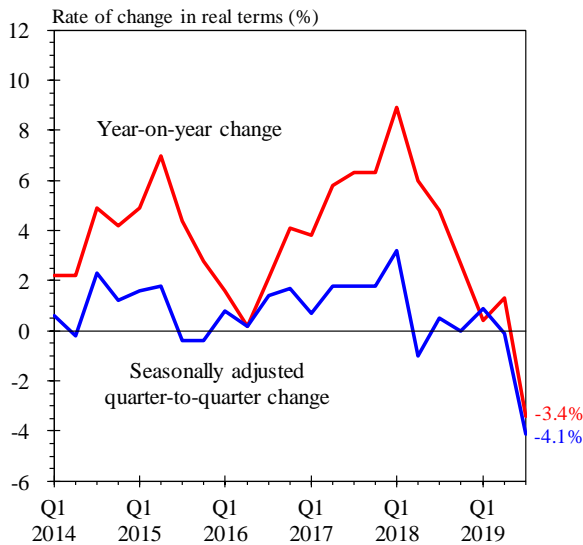
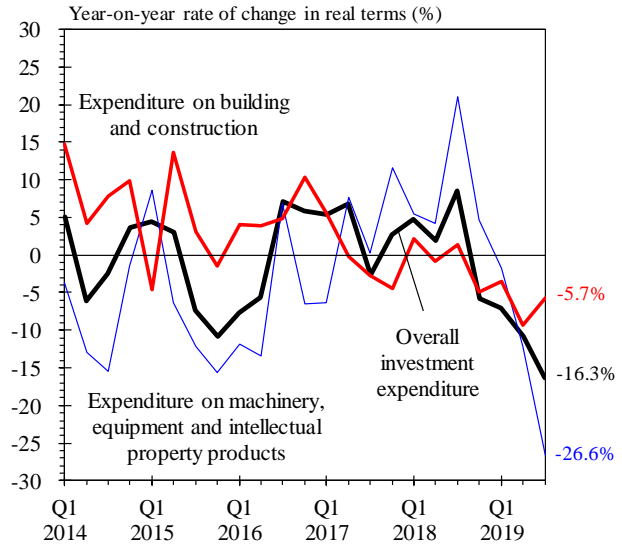


Chart 3(b) : Overall investment spending registered a widening decline

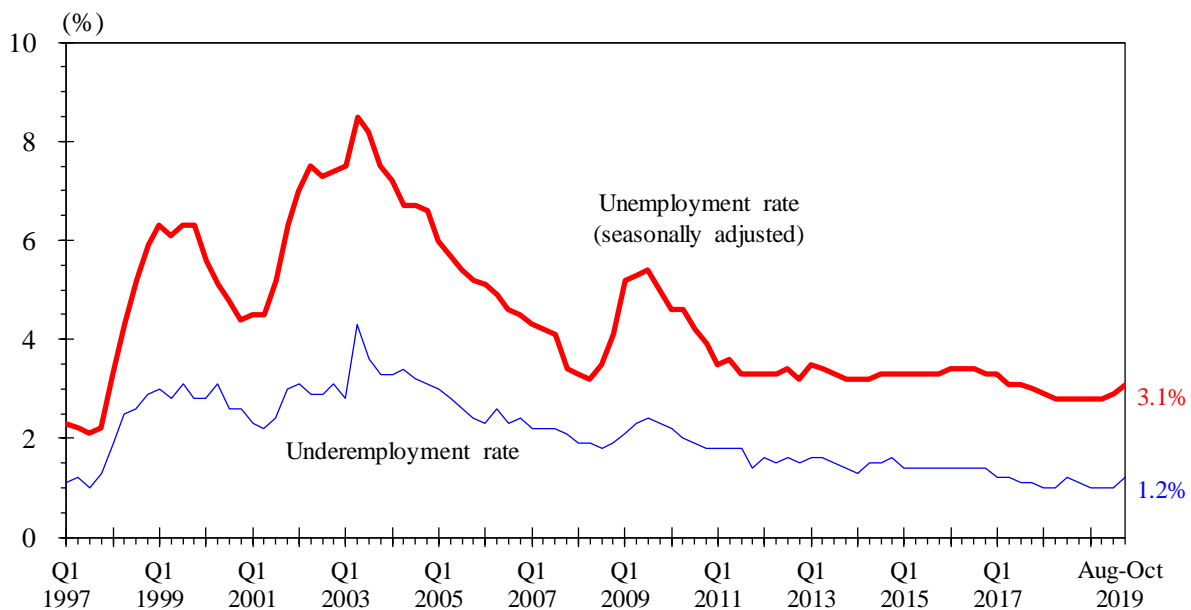


8. As for external direct investment (DI), the total stock of inward DI amounted to \$16.4 trillion at end-June 2019, equivalent to 5.7 times GDP. According to the latest available figures analysed by source, at end 2017, the Mainland continued to be a major source of inward DI, accounting for around 25% of the total stock. Separately, according to the survey results for 2019, the number of business operations in Hong Kong with parent companies either overseas or in the Mainland climbed to a new record high of 9 040 as at 3 June, reflecting Hong Kong’s business friendly environment as well as its prominent role as a conduit between the Mainland and the rest of the world. Hong Kong was ranked the world’s third easiest place to do business by the World Bank’s *Doing Business Report* published in October.

Labour Market

9. The labour market eased further as economic conditions continued to worsen. The seasonally adjusted unemployment rate edged up to 2.9% in the third quarter of 2019 and increased further to 3.1% in August – October, after staying at 2.8% for five quarters since the second quarter of 2018. The underemployment rate likewise increased to 1.2% in August – October after staying at a low level of 1.0% in the first three quarters (Chart 4). The unemployment rates in the consumption- and tourism-related sectors, which were hard hit by the local social incidents and violent acts, saw more visible increases. Reflecting signs of easing labour demand even before the local social incidents, private sector employment as enumerated from establishments declined in June 2019 for the first time in almost a decade along with a noticeable drop in vacancies.

Chart 4 : The labour market eased further

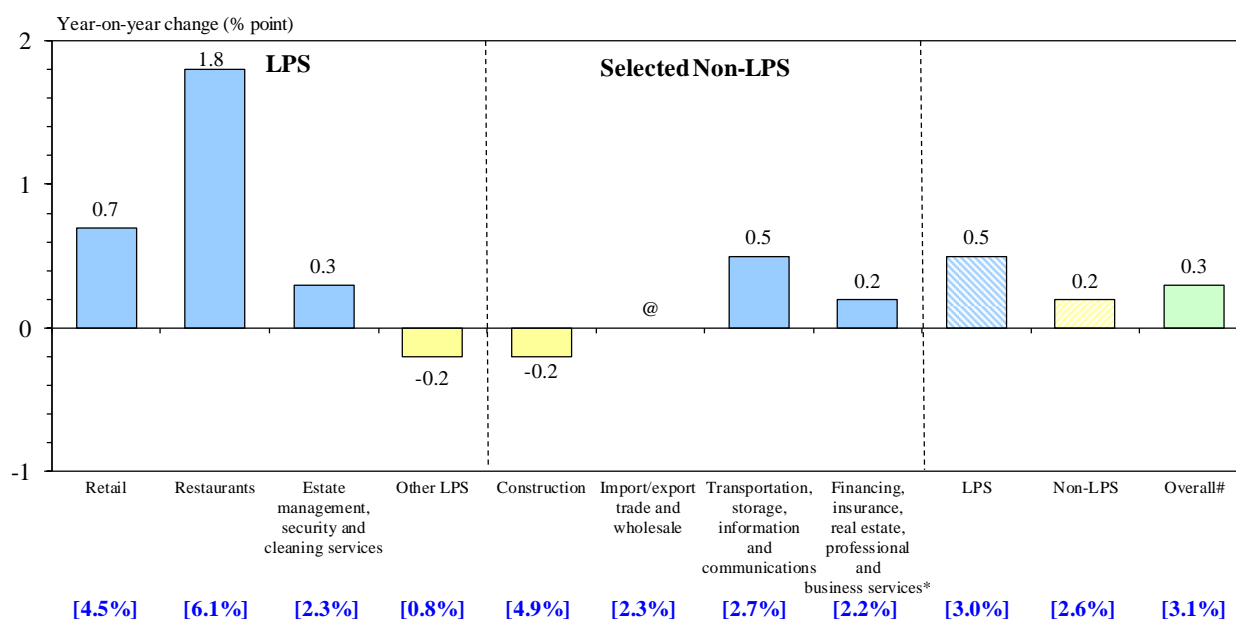


10. In August – October 2019, the unemployment rate of the low-paying sectors (LPS)⁽²⁾ as a whole rose by 0.5 percentage point from a year earlier to 3.0% (Chart 5). The unemployment rate surged in some sectors within the LPS due to the severe impacts of the local social incidents and violent acts. The unemployment rate of the restaurants sector rose sharply by 1.8 percentage points from a year earlier to 6.1%, the highest in more than six years, while that of the retail sector also increased by 0.7 percentage point from a year earlier to 4.5%, the highest level in more than two years.

(2) The fourth-term 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.

Meanwhile, the unemployment rate of the non-LPS went up by 0.2 percentage point to 2.6%. Although the unemployment rate of the construction sector went down by 0.2 percentage point from a year earlier and that of the import/export trade and wholesale sector showed little change from its level a year ago, employment in these two sectors continued to decline amid falling construction activities and shrinking trade flows respectively. Analysed by skill segment, the unemployment rate of higher-skilled workers increased by 0.2 percentage point from a year earlier to 2.0%, while that of lower-skilled workers also increased by 0.3 percentage point from a year earlier to 3.2%.

Chart 5 : Unemployment rates of the retail and restaurants sectors rose visibly from a year earlier



Notes: Figures in square brackets refer to the unemployment rate for that sector in Aug-Oct 2019 (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.

(@) Change less than 0.05 percentage point.

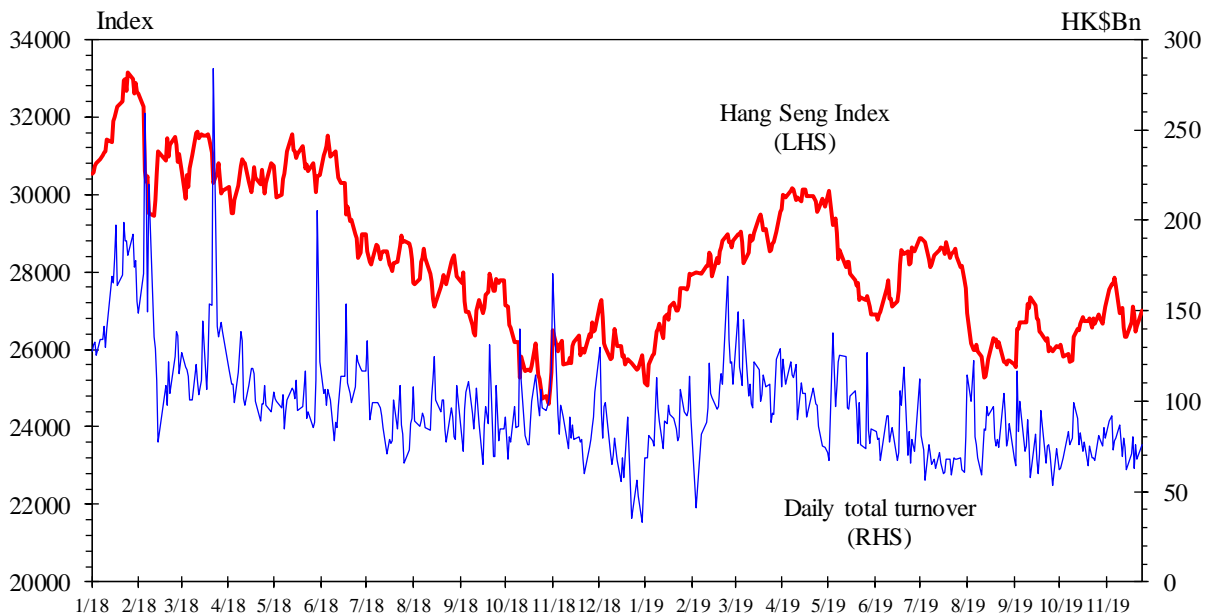
11. Nominal wages and earnings stayed on the rise in the second quarter. Nominal wages rose by 3.8% over a year earlier in June, and nominal payroll increased by 4.1% in the second quarter. Wages and earnings recorded solid gains in many sectors, yet those in import/export trade and wholesale and in retail trade continued to see relatively modest increases. More recent statistics as compiled from household surveys showed that the average monthly employment earnings of full-time employees (excluding foreign domestic helpers) of the lowest three decile groups combined increased by 3.8% year-on-year in nominal terms in the third quarter, similar to their 3.7% increase in the second quarter. However, the increase was somewhat lower than the Consumer Price Index (A) inflation rate of 3.9% in the third quarter. Separately, the average monthly employment earnings of all full-time employees (excluding foreign domestic helpers) increased by 4.7% year-on-year in nominal terms in the third quarter, visibly slower than their 8.4% growth in the second quarter. Meanwhile, the median monthly household income (excluding foreign

domestic helpers) slipped to a year-on-year decline of 1.0% in nominal terms in the third quarter from an increase of 5.6% in the second quarter, partly reflecting the high base of comparison in the same quarter last year (when there was a year-on-year increase of 8.4%) and the drag from demographic changes. Another factor was the abruptly worsened economic situation in the third quarter, although more observations would be needed to ascertain the extent of the impact. Please refer to *Annex* for details on the recent situation of household income.

Asset markets

12. Along with the fluctuations in US-Mainland trade relations, the local stock market has been volatile after staging a rebound in the first four months of 2019. The Hang Seng Index (HSI) has undergone a sharp correction since May amid the softening global economic growth and the ongoing local social incidents, though it has gained slightly recently in view of possible first-phase trade agreement between the Mainland and the US. The HSI fell by 12.1% during May – September of 2019, but subsequently rebounded to 26 993 on 25 November (*Chart 6*). The average daily turnover of the stock market fell to \$81.0 billion during May – October from \$101.8 billion in the first four months this year.

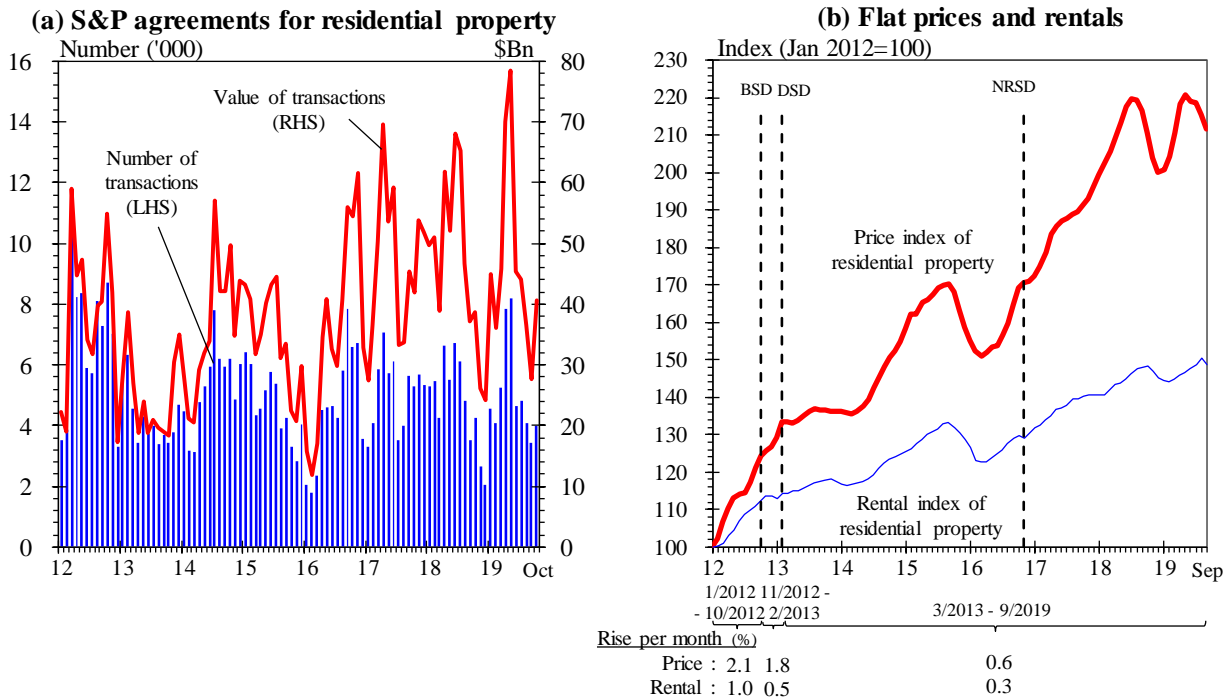
Chart 6 : The local stock market has been volatile



13. The residential property market softened during the third quarter, as sentiment was dampened by the prolonged local social incidents and violent acts, US-Mainland trade tensions and weaker global economy. The monthly average number of sale and purchase agreements for residential property received by the Land Registry fell to 4 084 in July to October, well below its monthly average of 5 753 registered in the first half of 2019 (*Chart 7(a)*).

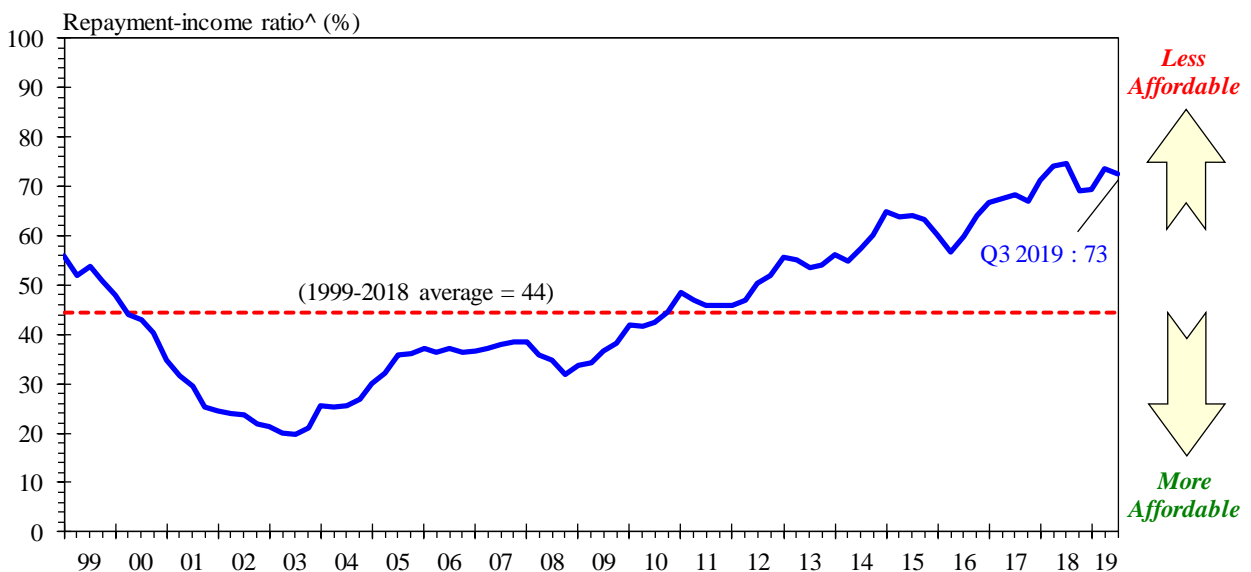
14. Flat prices on average in September declined by 3% from June, and were 4% lower than their recent peak in May. Between June and September, flat rentals on average edged up by 1%. Nonetheless, during the first three quarters of 2019, flat prices and rentals still rose by 6% and 2% respectively (*Chart 7(b)*).

Chart 7 : The residential property market softened during the third quarter



15. Notwithstanding their recent decline, flat prices in September 2019 still exceeded the 1997 peak by 120%. The index of home purchase affordability (i.e. the ratio of the mortgage payment for a 45-square metre flat to the median income of households, excluding those living in public housing) remained elevated at around 73% in the third quarter of 2019, significantly above its long-term average of 44% over 1999-2018 (*Chart 8*).

Chart 8 : The index of home purchase affordability remained elevated



Note : (^) The ratio of the mortgage payment for a flat with saleable area of 45 sq m (assuming 70% loan-to-value ratio and tenor of 20 years) to the 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.

16. Raising the flat supply by increasing land supply is a key policy of the Government. In September, the Government announced it would put up two residential sites for sale in the fourth quarter of 2019. Combining the various sources (including Government land sales, railway property development projects, and private development and redevelopment projects), the total private housing land supply in the first three quarters of 2019-20 is estimated to have the capacity to produce about 9 230 units. The total supply of flats in the private sector 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) would stay at a high level of 93 000 units as estimated at end-September. In October, the Chief Executive announced various measures and plans on housing and land supply in her Policy Address.

17. Over the past several years, the Government has also implemented demand-side management and macroprudential measures to dampen speculative, investment and non-local demand, and to reduce the possible risks to financial stability arising from an exuberant property market. These measures have yielded notable results. On speculative activities, the number of short-term resales (comprising confirmor transactions and resales within 24 months after assignment) remained low at 61 cases per month or 1.1% of total transactions in the first ten months of 2019, 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*). Purchases by non-local individuals and non-local companies also stayed low at 53 cases per month or 0.9% of total transactions in the first ten months of 2019, much lower than the monthly average of 365 cases or 4.5% in January to October 2012 (i.e. the period before the introduction of the Buyer's Stamp Duty) (*Chart 10*). As an indicator of investment activities, purchases subject to the New Residential Stamp Duty stayed at a modest level of 403 cases per month or 7.2% of total transactions in the first ten months of 2019, markedly lower than the monthly average of 1 412 cases (or 26.5%) subject to Double Stamp Duty in January to November 2016 (*Chart 11*). As for mortgage lending, the average loan-to-value ratio of new mortgages was 47% in January to September 2019, likewise considerably below the average of 64% in January to October 2009 before the first round of macroprudential measures for residential property mortgage lending was introduced by the Hong Kong Monetary Authority.

Chart 9 : Short-term speculative activities stayed subdued

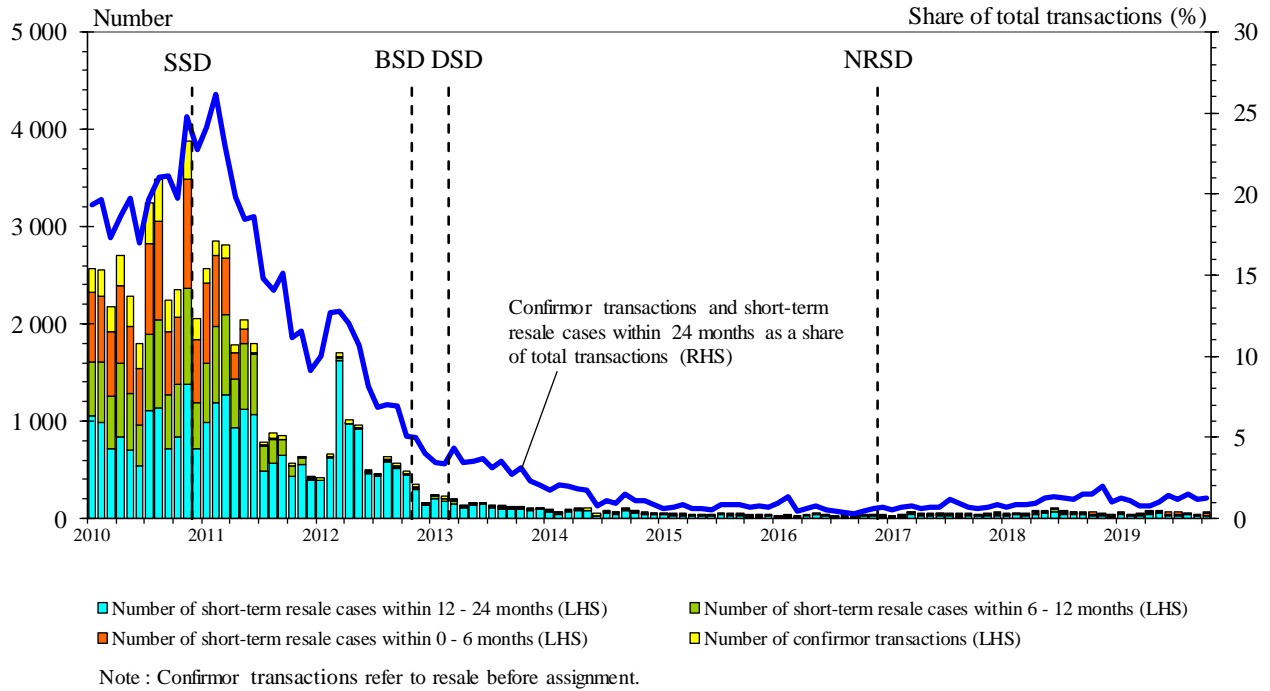


Chart 10 : Purchases by non-local buyers remained low

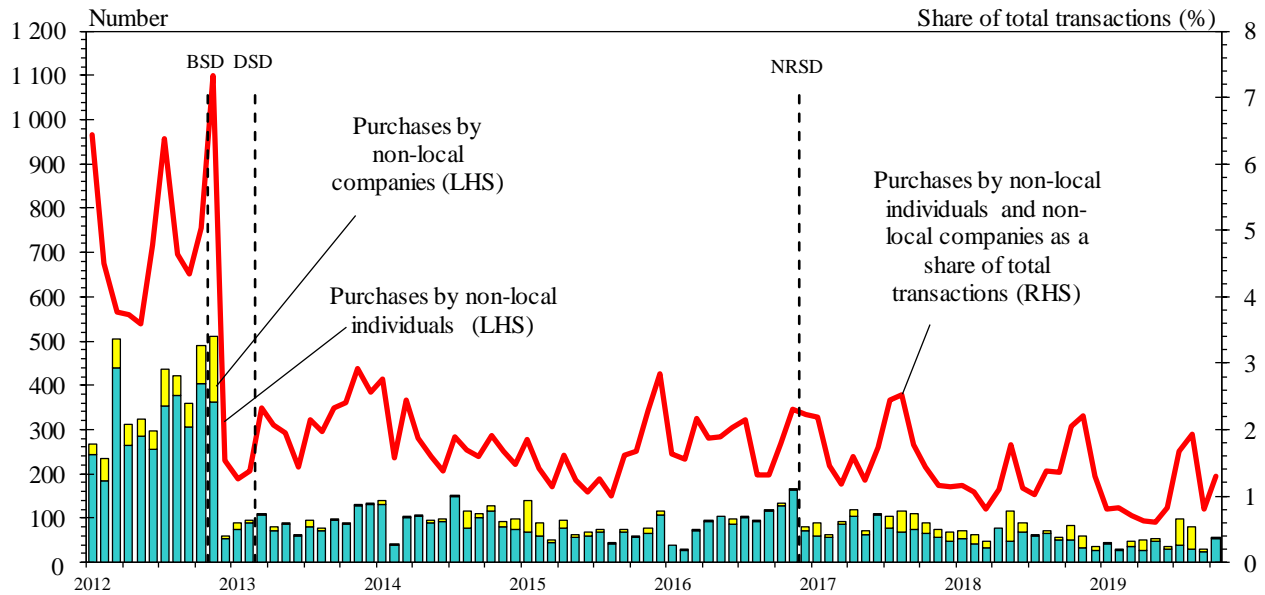
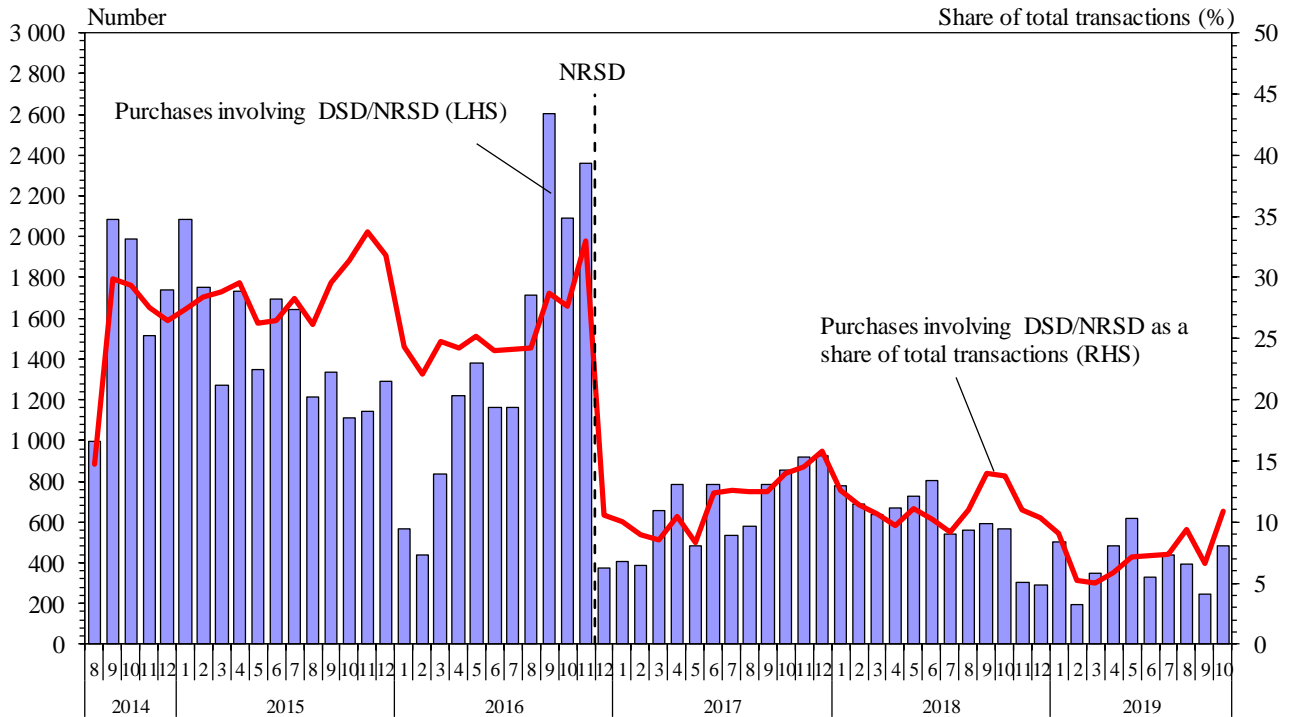
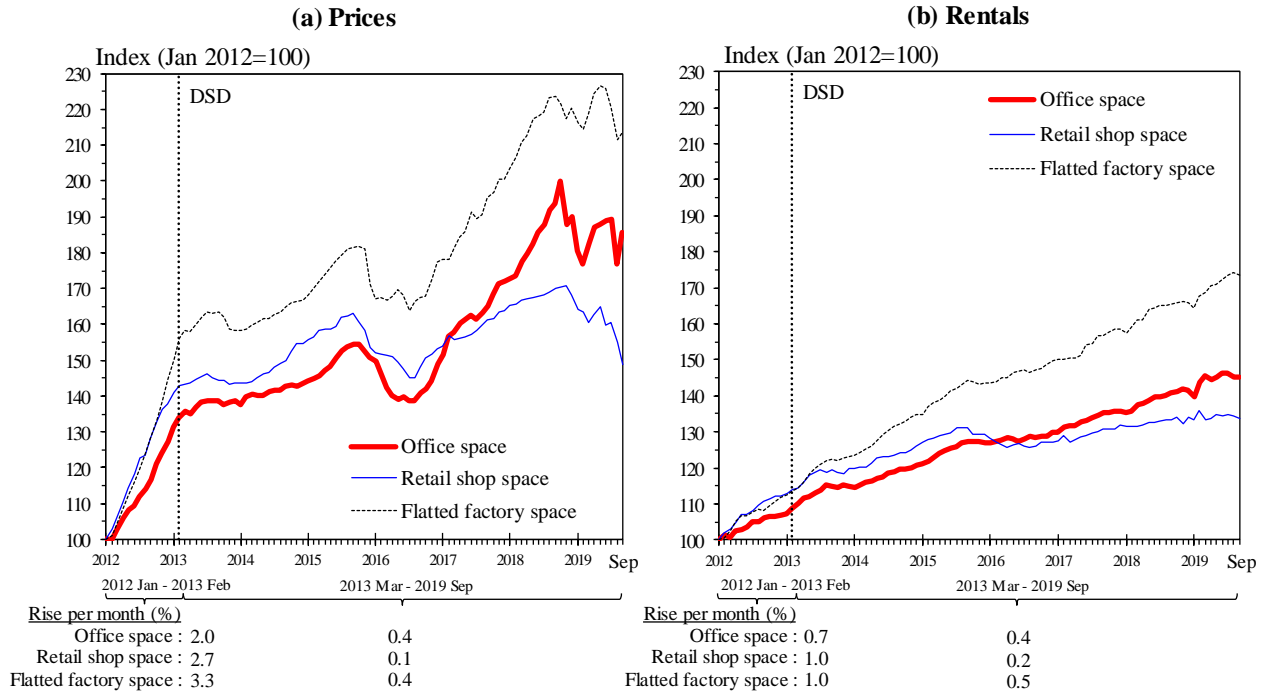


Chart 11 : Investment activities were modest



18. Amid subdued local economic conditions, the commercial and industrial property markets also turned quieter in the third quarter. Sale prices and rentals of office space on average decreased by 2% and 1% respectively between June and September. For retail shop space, sale prices declined by 7% between June and September, while rentals were little changed. As for flatted factory space, sale prices fell by 5%, while rentals increased by 1% (*Chart 12*). Trading activities for these market segments in the third quarter fell markedly from the preceding quarter.

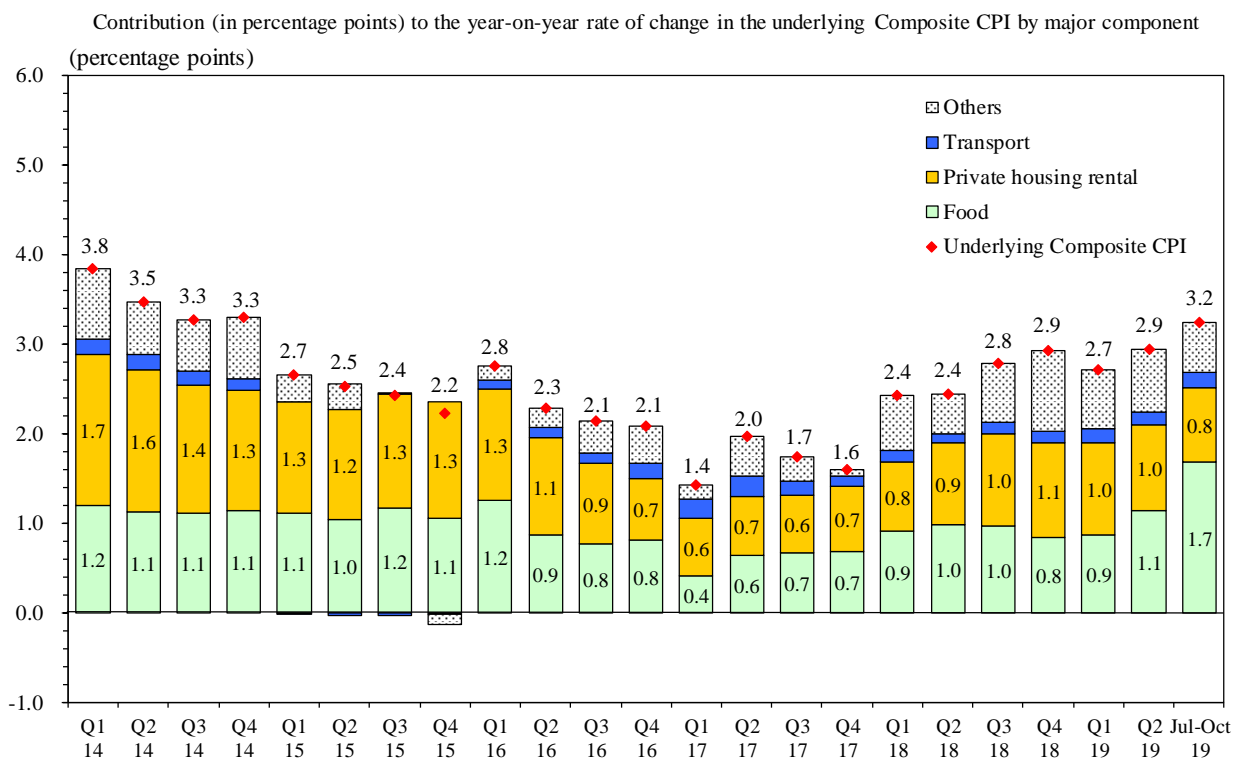
Chart 12 : Prices of non-residential properties decreased during the third quarter, while rentals exhibited diverse movements



Inflation

19. Consumer price inflation went up further in recent months, mainly reflecting the visible acceleration in the increase in prices of basic foodstuffs amid the reduced supply of fresh pork. Price pressures on other major consumer price index components remained largely moderate. Netting out the effects of the Government’s one-off relief measures to more accurately reflect the underlying inflation trend, underlying consumer price inflation rose from 2.9% in the second quarter to 3.2% in July – October 2019, and averaged 3.0% in the first ten months combined (*Chart 13*).

Chart 13 : Consumer price inflation went up further in recent months



20. Analysed by major component of the underlying Composite Consumer Price Index (Composite CPI) (*Table 1*), prices of food, the component with the largest weight other than housing, rose at a faster year-on-year rate of 6.1% in July – October 2019, within which prices of basic foodstuffs rose visibly by 13.4% due to the surge in pork prices, the largest increase since the fourth quarter of 2008. The surge in pork prices directly contributed 1.0 percentage point to the underlying inflation rate of 3.2% in July – October. On the other hand, the rise in the private housing rental component narrowed to 2.7%. The increase in the public housing rental component has moderated notably since September as the effect of upward adjustment in public housing rentals in September last year began to dissipate. Meanwhile, prices of miscellaneous goods and transport rose moderately. Prices of electricity, gas and water, and of miscellaneous services saw moderated upward pressure, with the latter due to the smaller increase in charges for package tours. Prices of clothing and

footwear continued to fall, while prices of durable goods stayed on a secular downtrend.

Table 1 : Underlying Composite Consumer Price Index by component
(year-on-year rate of change, %)

<u>Expenditure component</u>	<u>Weighting (%)</u>	<u>2018</u>	<u>2018</u>				<u>2019</u>		<u>Jul-Oct</u>
			<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	
Food	27.29	3.4	3.3	3.6	3.5	3.0	3.1	4.1	6.1
<i>Meals bought away from home</i>	17.74	2.9	3.0	3.0	2.9	2.6	2.3	2.1	2.1
<i>Other foodstuffs</i>	9.55	4.3	3.8	4.9	4.8	3.7	4.6	7.7	13.4
Housing ^(a)	34.29	3.2 (2.5)	2.5 (2.5)	2.9 (2.0)	3.4 (2.5)	3.9 (3.0)	3.9 (2.9)	3.6 (4.2)	2.9 (3.5)
<i>Private housing rent</i>	29.92	3.1 (2.2)	2.5 (2.5)	3.0 (1.9)	3.4 (2.3)	3.4 (2.4)	3.4 (2.3)	3.1 (3.8)	2.7 (3.3)
<i>Public housing rent</i>	1.94	3.6 (4.1)	0.1 (0.4)	0.5 (0.4)	3.6 (4.1)	10.1 (11.6)	10.1 (11.6)	9.8 (10.9)	4.9 (5.1)
Electricity, gas and water	2.67	4.7 (4.9)	8.4 (8.3)	3.5 (3.7)	3.6 (3.8)	3.7 (4.0)	1.4 (-4.9)	1.5 (-4.8)	0.8 (-5.6)
Alcoholic drinks and tobacco	0.54	1.3	0.3	0.6	1.7	2.7	2.7	2.4	0.2
Clothing and footwear	3.21	1.6	2.3	2.0	2.3	0.1	-0.2	-1.7	-2.0
Durable goods	4.65	-2.0	-2.1	-2.1	-2.0	-1.9	-2.1	-2.0	-1.5
Miscellaneous goods	3.56	1.3	1.1	1.3	1.5	1.4	1.6	2.0	3.0
Transport	7.98	1.6	1.7	1.3	1.7	1.7	1.9	2.0	2.2
Miscellaneous services	15.81	2.1	1.7	1.4	2.1	3.1	1.9	2.5	2.0
All items	100.00	2.6 (2.4)	2.4 (2.4)	2.4 (2.1)	2.8 (2.5)	2.9 (2.6)	2.7 (2.2)	2.9 (3.0)	3.2 (3.3)

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

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

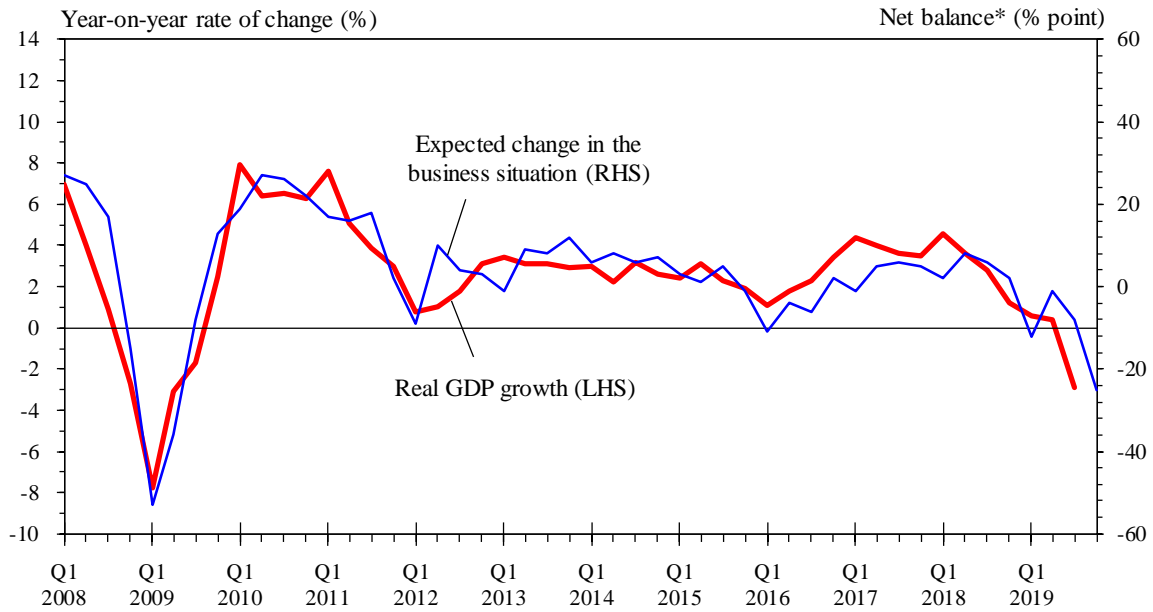
Updated economic forecasts for 2019

21. The global economy has been in a synchronised slowdown so far this year. Recent data revealed that the growth momentum of major economies has moderated further. Although US-Mainland trade tensions have eased somewhat of late, there may still be twists and turns in US-Mainland trade relations as the two sides have yet to resolve differences in certain key areas. The development of Brexit will be affected by the general election results and is still subject to many uncertainties, whereas geopolitical risks in the Middle East have shown signs of escalation and warrant attention. Amid an austere external environment in the near term, Hong Kong's export performance is expected to remain weak.

22. Domestically, the local social incidents with increasing violence over the past few months have greatly affected tourists' intention to visit Hong Kong, taken a heavy toll on local consumption, and seriously dampened economic sentiment. All the recent establishment surveys indicated that local business sentiment has turned very pessimistic (*Chart 14*). If the adverse impacts of violent acts and the local social incidents on domestic demand cannot abate, local consumption and investment demand will likely remain in the doldrums for the rest of the year.

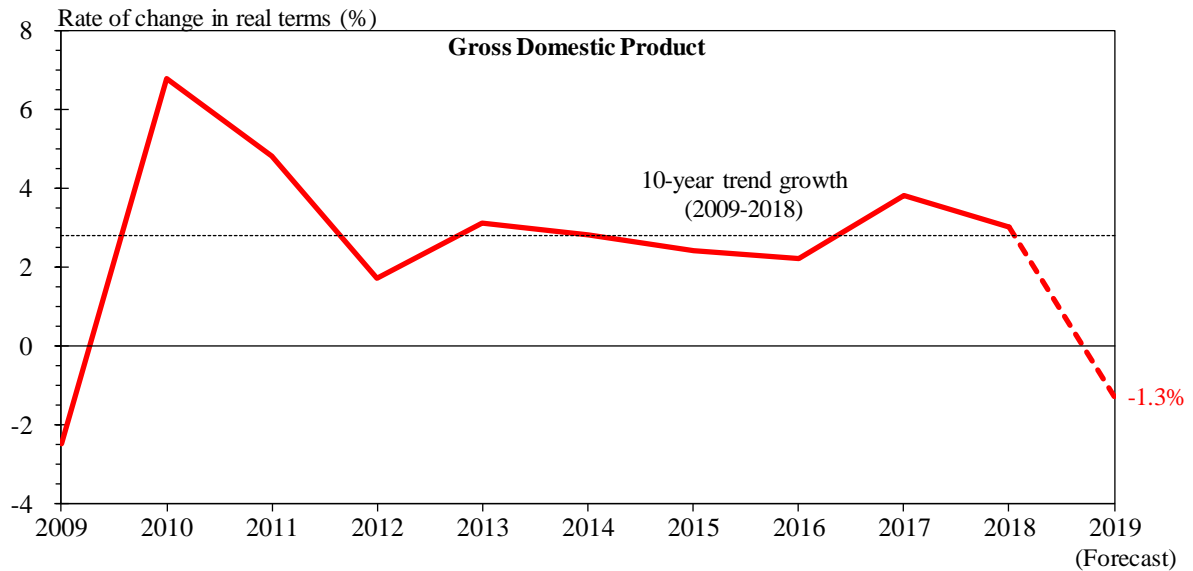
23. Taking into account the year-on-year contraction of 0.6% in the first three quarters combined and the still notable downward pressures, the Hong Kong economy is forecast to contract by 1.3% for 2019 as a whole, marking the first annual decline since 2009 (*Chart 15*). The Government will continue to closely monitor developments on the domestic and external fronts, as well as their impacts on people's livelihood and employment, and will introduce appropriate measures when necessary to support enterprises and safeguard jobs. For reference, the latest forecasts of Hong Kong's economic growth in 2019 by the IMF and private sector analysts ranged from -2.1% to +0.7%.

Chart 14 : Business sentiment among large enterprises has turned pessimistic



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.

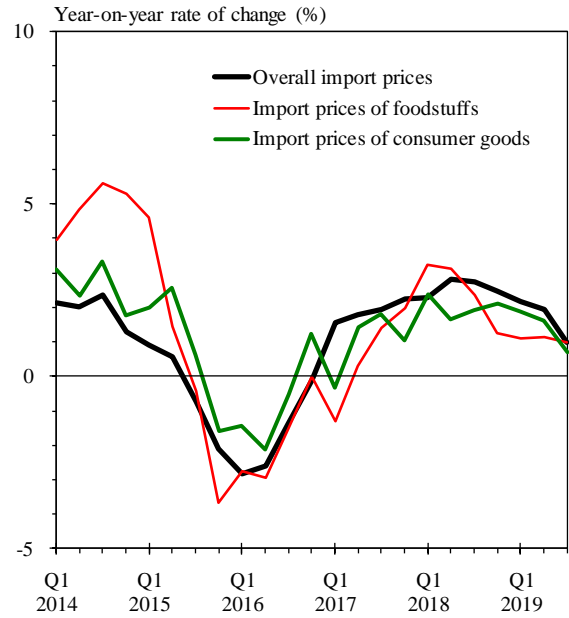
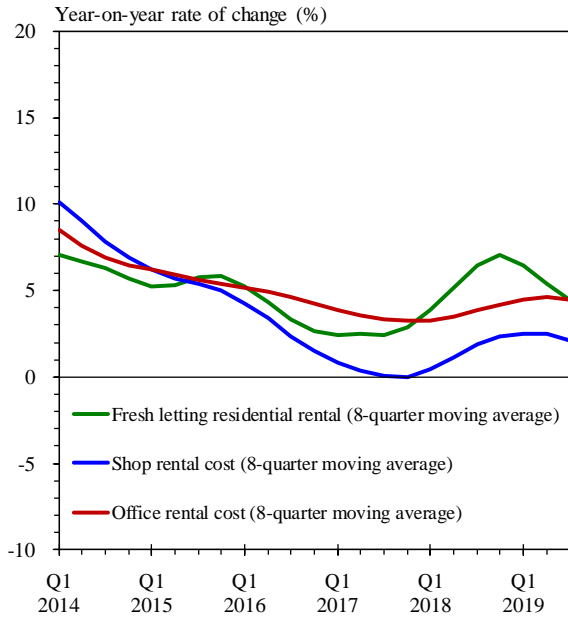
Chart 15 : Economy is forecast to contract by 1.3% for 2019 as a whole



24. On inflation, the underlying and headline consumer price inflation rates for the first ten months of 2019 averaged 3.0% and 2.9% respectively. Overall price pressures in the rest of 2019 should remain contained along with subdued local economic conditions and further easing of imported inflation. Yet, inflation may stay somewhat elevated in the near term given the supply situation of fresh pork (**Chart 16**). Taking into account the actual outturns so far this year, the forecasts of underlying and

headline consumer price inflation for 2019 as a whole are 3.0% and 2.9% respectively. For reference, the forecasts of Hong Kong's consumer price inflation for 2019 by the IMF and private sector analysts ranged from 2.5% to 3.0%.

Chart 16 : Local cost pressures were largely contained while external price pressures eased further

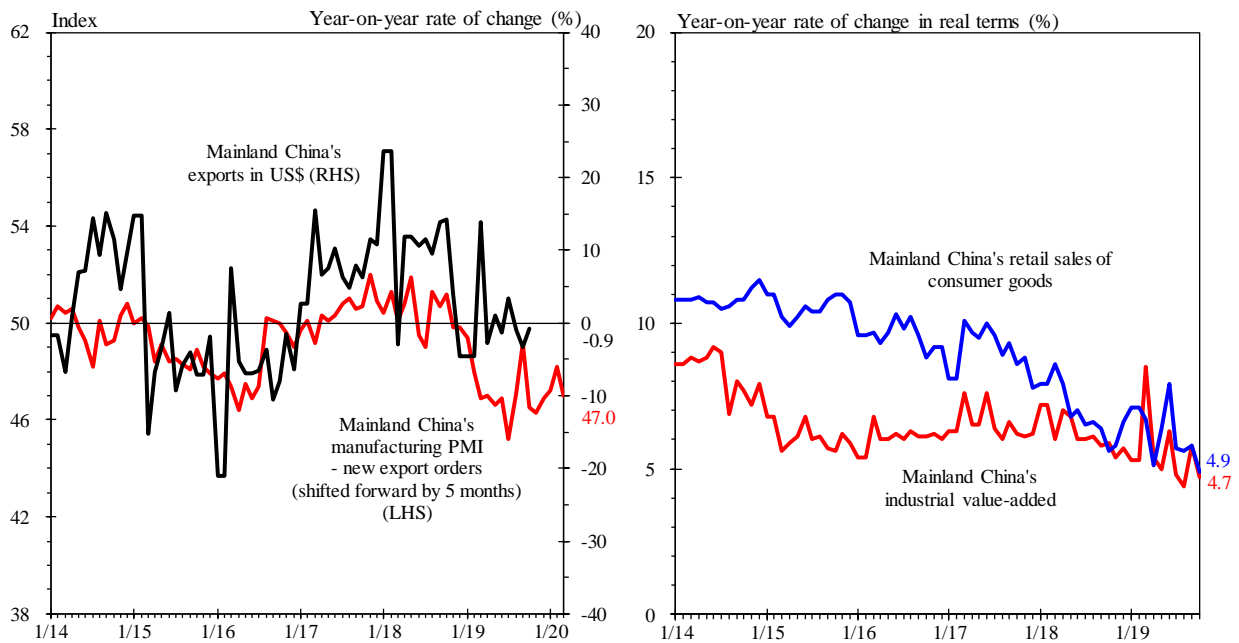


Economic outlook for 2020

25. The market remains cautious about the global economic outlook for 2020. In mid-October the IMF forecast that global economic growth would pick up somewhat from 3.0% in 2019 to 3.4% in 2020. Yet, it is expected that the growth of several major economies would moderate further, indicating that the recovery is not broad-based and is fraught with uncertainties. In particular, the IMF projected that advanced economies would grow by 1.7% in 2020 (the projected growth for 2019 also at 1.7%), and that emerging and developing Asia would grow by 6.0% (slightly higher than the projected growth of 5.9% in 2019).

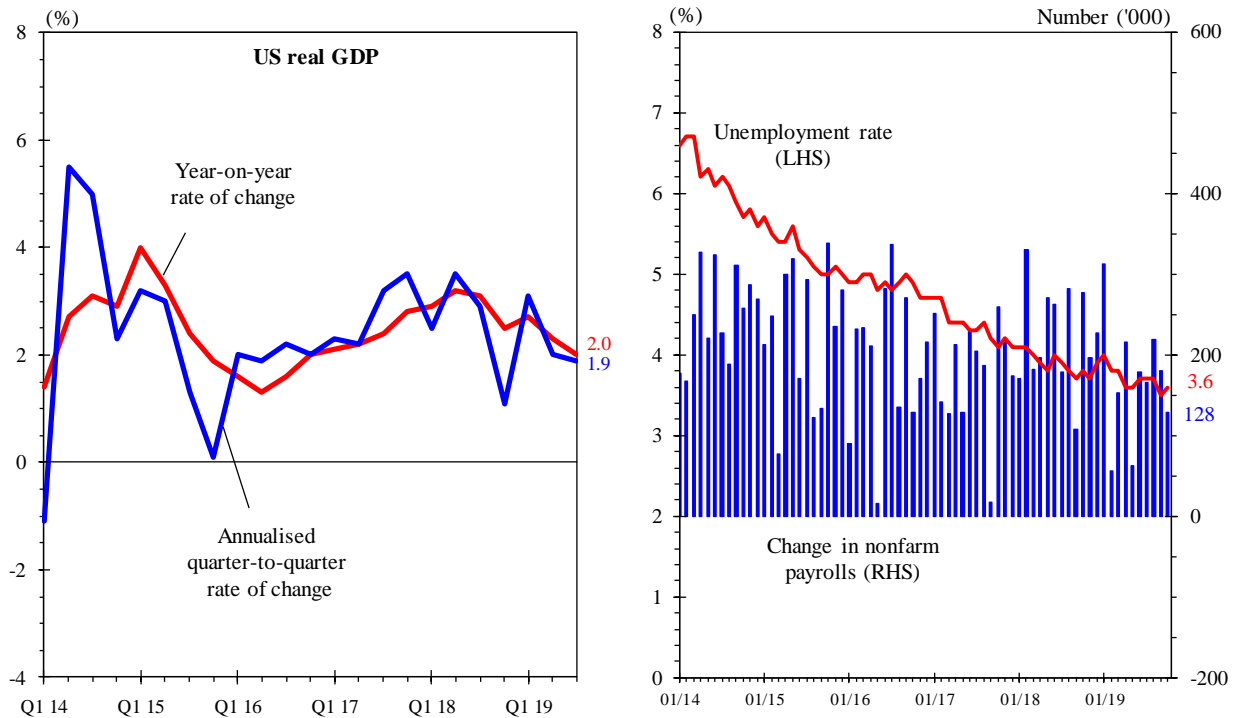
26. The Mainland economy registered resilient growth of 6.2% in the first three quarters of 2019 and is expected to stay on track to attain the full-year official growth target of 6 – 6.5%. Growth in retail sales and the employment situation remained broadly stable in recent months. Yet, export activities have gradually slowed down so far this year due to sluggish external demand and US-Mainland trade tensions. As indicated by the latest figures for October, growth in fixed asset investment was at a low level, while official manufacturing and non-manufacturing PMIs both fell, indicating weakening confidence in business prospects among enterprises (*Chart 17*). While US-Mainland trade tensions have eased somewhat as negotiations are underway for sealing a first-phase trade agreement, they are still subject to uncertainties and the impact on the Mainland's export performance next year is not clear. The IMF projected the Mainland's economic growth to moderate further to 5.8% in 2020. Nonetheless, being the world's second largest economy, the economic fundamentals of the Mainland are still stable, and its growth rate will continue to be much higher than other major economies. The Mainland authorities have also rolled out a series of measures, covering aspects such as fiscal, monetary, and employment support and consumption boosting, to support economic development.

Chart 17: The Mainland economy stayed on track to attain the full-year official growth target in 2019



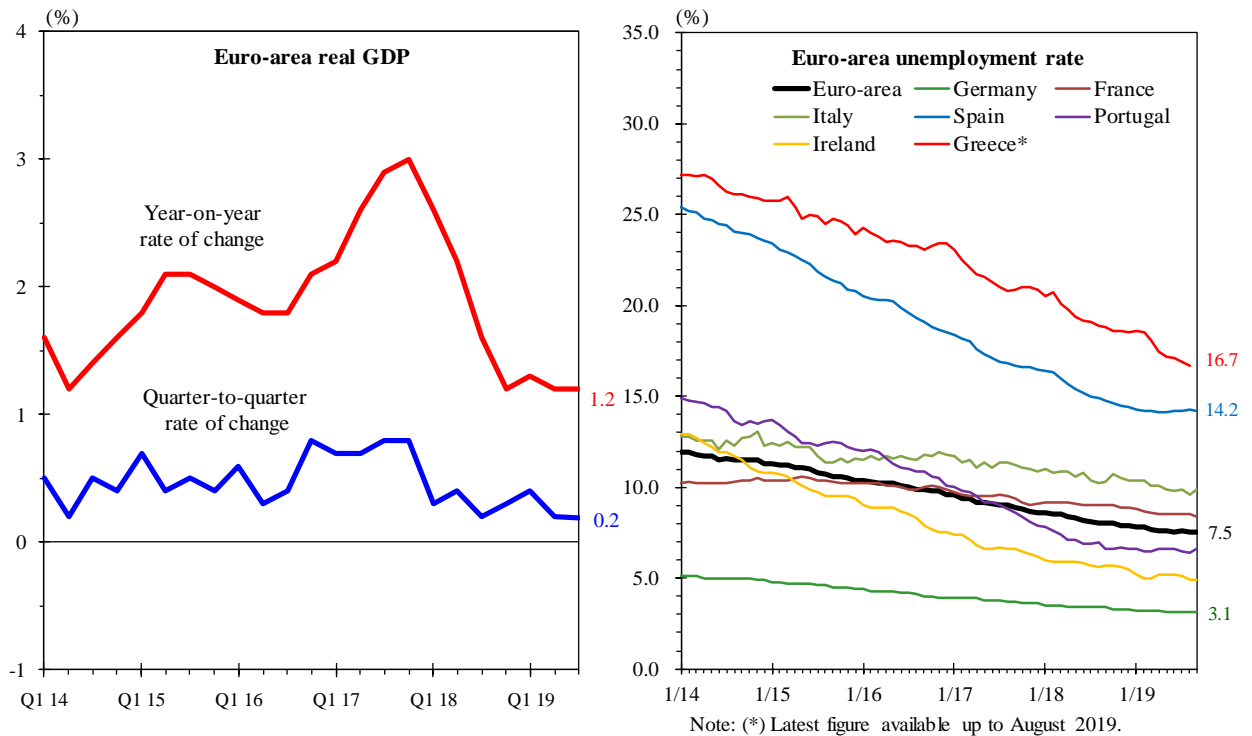
27. The economic growth of the US slowed down gradually in 2019, from 2.5% year-on-year in the first half of the year to 2.0% in the third quarter (*Chart 18*), partly reflecting that the boost from earlier fiscal stimulus were fading. Economic sentiment in the US has also turned cautious in recent months. The expected shift in the US' fiscal stance from expansionary in 2019 to broadly neutral in 2020, together with fluctuations in US trade policy, will likely increase uncertainties facing the US economy. Yet, the US labour market held resilient, with the unemployment rate staying low, will render support to private consumption. Furthermore, given the US presidential election next year, it remains to be seen whether the US will roll out fresh fiscal stimulus to support the economy.

Chart 18 : Economic growth of the US slowed down gradually, but the US labour market held resilient



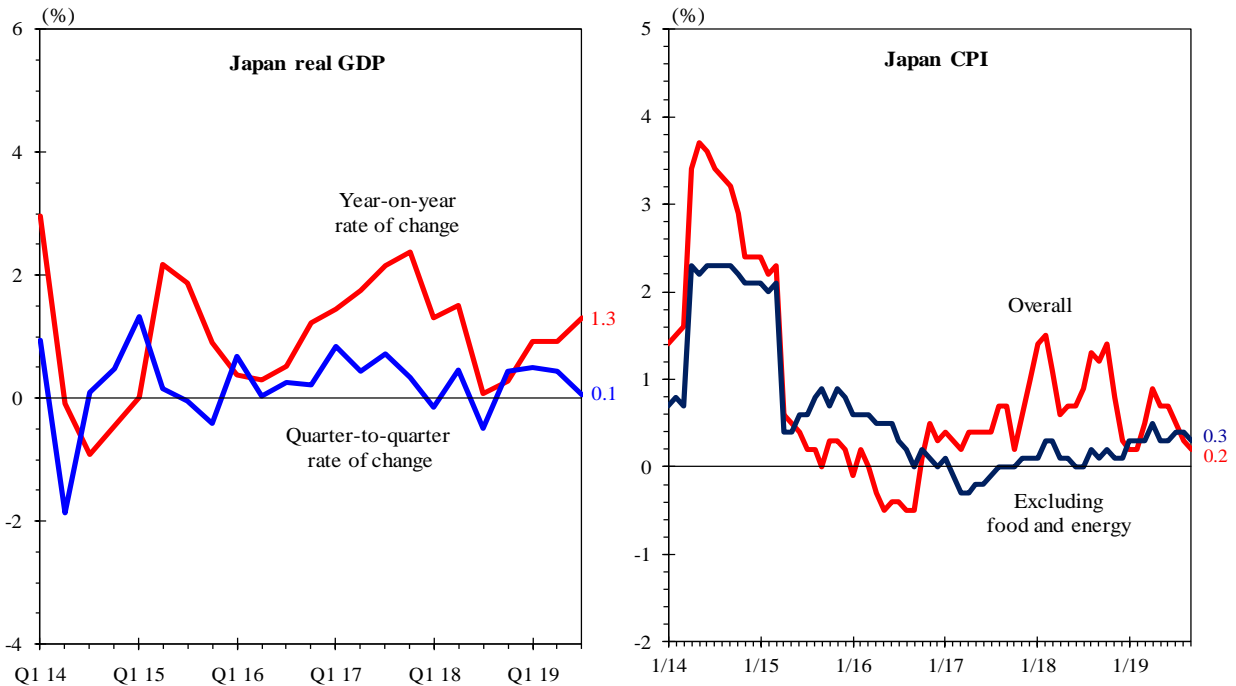
28. Regarding the euro area, economic growth remained slow thus far, at 1.2% year-on-year in the first three quarters of 2019 combined (*Chart 19*). In particular, the economic growth of the major member states, including Germany, France and Italy, remained soft. Business sentiment in the region was subdued. The manufacturing PMI in the euro area was in the contractionary zone most of the time in 2019, reflecting subdued production activities. Industrial production kept registering year-on-year declines in the year, while the declines widened in the second half of the year. Inflation in the euro area hovered around a three-year low, far below the European Central Bank’s (ECB) target of near 2%. The deadline for Brexit was extended further several times. Future development depends on the results of the upcoming general election and other domestic factors, and the possibility of a no deal Brexit cannot be ruled out completely. Other developments, such as political issues in Spain and the social unrest in France, may also have implications for financial stability of the region and warrant attention.

Chart 19 : The euro area's economic growth remained slow in 2019 so far



29. Japan's economy grew modestly in the first three quarters of 2019 (*Chart 20*). The consumption tax hike in October may further increase the downward pressure on Japan's economy in the near term, though the fiscal stimulus put forward by the Japanese government earlier on could partly offset the adverse impacts. As Japan's economy would remain constrained by sluggish external demand and various structural issues such as population ageing and elevated public debt, economic growth is expected to remain subdued. As for the rest of Asia, economic growth of many economies also eased in the first three quarters compared to the previous year amid weakening exports. The growth prospects for Asian economies in 2020 inevitably will continue to be affected by the various headwinds in the global economic environment.

Chart 20 : Japan's economy grew modestly in 2019 so far, while inflation still remained low



30. Due to a broad-based deterioration of global trade and manufacturing activities, the global economic outlook is still facing various difficulties with downside risks remaining notable. Many major central banks have taken steps to ease monetary policies to cope with the situation. The US Federal Reserve has cut its target range for the federal funds rates three times since July, to 1.5 – 1.75%, and Fed Chairman Powell repeatedly said that the current stance of monetary policy would continue. In September, the ECB cut its deposit facility rate by 0.1 percentage point to -0.5% and launched a new round of bond buying programme starting from November for an unlimited period. In Asia, the Bank of Japan continued its loose monetary policy, keeping its short-term interest rate target at -0.1% and the 10-year government bond yield at around zero. The Monetary Authority of Singapore eased its monetary policy in October, the first time since April 2016. Various central banks in emerging market economies have lowered their policy rates several times so far this year, with a view to supporting economic growth. While these measures may help cushion the impact of various headwinds on their own economies, the various central banks would have limited room for rolling out further monetary stimuli if downward risks intensify.

31. Amid the highly uncertain external environment, Hong Kong's economic outlook for 2020 is fraught with uncertainties. The risks of trade barriers and geopolitical tensions could further disrupt global supply chains and hit global economic confidence, investment and economic growth. If the downside risks intensify, there could be an abrupt shift in market sentiment, triggering gyrations in global financial markets and dampening economic sentiment in Hong Kong. Furthermore, Hong Kong's export performance would unavoidably be affected by the

expected moderation of economic growth in many of Hong Kong's major trading partners. If the Mainland and the US could seal a first-phase trade agreement in the near term and partly remove the tariffs, global economic sentiment would probably show some improvement.

32. Ongoing local social incidents and violence are another risk factor that warrants attention. If demonstrations involving violence persist, they will pose a more severe drag on the consumption- and tourism-related sectors. Foreign investors' and local citizens' confidence in the Hong Kong economy will be dampened further, adding downward pressures on private consumption and investment in the coming year. If the situation continues, other sectors will also be affected, and the local labour market will be subject to increasing pressure. Ending violent acts is pivotal to the people's livelihood and the recovery of the Hong Kong economy.

33. Hong Kong's inflation outlook will hinge on a host of factors, including overall economic growth, local cost pressures, inflation in our major import sources, international commodity prices, etc. It will take time for the supply of live pigs to return to normal levels. If pork prices continue to increase in the near term, overall consumer price inflation may stay somewhat elevated at the beginning of 2020. Given that global inflation will likely remain moderate, external price pressures should be contained. The local cost pressures will depend on economic performance and the movement of private residential rentals.

34. The Government will closely monitor the developments on the domestic and external fronts and announce the economic growth and inflation forecasts for 2020 along with the 2020-21 Budget in February 2020. For reference, the latest forecasts of Hong Kong's economic growth for 2020 by the IMF and most of the private sector analysts were in the range of -0.7% to +1.7%, while those of consumer price inflation were in the range of 1.8% to 2.6%.

Office of the Government Economist
Financial Secretary's Office
25 November 2019

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. The benchmark of monthly household income for low-income households is adjusted by inflation⁽²⁾ to increase from \$8,800 (at constant Q2 2019 prices) to \$8,900 (at Q3 2019 prices), so as to reflect the latest circumstance.

Overall situation of household income and employment earnings

2. In tandem with the deterioration in local economic environment in the third quarter of 2019, the local labour market also eased of late. Latest statistics showed that the seasonally adjusted unemployment rate went up from its low level of 2.8% in the first half of this year to 3.1% in August – October. Total employment registered a year-on-year decline of 0.6%, reflecting an easing in the overall labour demand.

3. Notwithstanding these, in the third quarter of 2019, the average employment earnings of full-time employees (excluding bonus) still rose by 4.0% year-on-year in nominal terms, or 0.6% in real terms after netting out inflation. The notably lower real increase was attributable to a higher inflation in the quarter driven up by the year-on-year surge in pork prices. Similarly for full-time unskilled employees, their average employment earnings increased by 2.3% in nominal terms but decreased by 1.5% in real terms. For higher-skilled staff, the latest 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 4.7% and 1.7% respectively in June 2019. On the other hand, median monthly household income, a reflection of the overall household income situation, saw a decrease of 1.0% year-on-year in nominal terms in the third quarter of 2019, or 4.2% in real terms (*Table 1*). This partly reflected a high base of comparison last year (8.4% nominal increase in the third quarter of 2018) and a higher share of economically inactive households amid continued population ageing. Another

(1) This Annex was originally provided in response to a Member's request at the meeting of the Panel on Financial Affairs on 5 December 2005. It has since been updated regularly for Members' information. Foreign domestic helpers are excluded from the analysis except general labour market statistics.

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

factor was the abruptly worsened economic situation in the third quarter of 2019, although more observations would be needed to ascertain the extent of such impact.

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

Period	Median monthly household income		Overall employment earnings of employees*		Employment earnings of unskilled employees^		Salaries of managerial and professional employees~		
2015	6.5	(3.4)	5.7	(2.6)	6.3	(2.2)	5.7	(3.8)	
2016	2.0	(-0.4)	6.1	(3.6)	5.7	(2.8)	5.2	(2.9)	
2017	5.0	(3.5)	4.3	(2.8)	5.5	(3.9)	4.9	(3.1)	
2018	Q1	7.7	(5.1)	6.3	(3.8)	4.5	(1.9)		
	Q2	5.3	(3.1)	5.6	(3.4)	6.5	(4.1)	4.8	(2.6)
	Q3	8.4	(5.8)	6.2	(3.6)	4.6	(1.8)		
	Q4	3.7	(1.1)	2.7	(0.1)	3.8	(0.6)		
2019	Q1	4.0	(1.8)	3.3	(1.1)	7.4	(4.6)		
	Q2	5.6	(2.5)	4.8	(1.7)	3.5	(0.1)	4.7	(1.7)
	Q3	-1.0	(-4.2)	4.0	(0.6)	2.3	(-1.5)		

Notes: (*) Average employment earnings of full-time employees (excluding bonus).
 (^) Average employment earnings of full-time employees.
 (~) The index is released annually for June.
 () Rate of change (%) in real terms.

Economically active households with monthly household income below \$8,900

4. In the third quarter of 2019, there were 71 900 economically active households with monthly household income below \$8,900 (referred to as “low-income households” thereafter). While up by 2 800 or 4.1% over a year earlier, its proportion in total domestic households stayed unchanged at 2.7%⁽³⁾.

5. An analysis of the number and proportion of low-income households over the past decade or so suggests that their changes in general 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 5.5% in the third quarter of 2003 to 3.2% in the third quarter of 2007. After the outbreak of the global financial tsunami in late 2008, the corresponding proportion rose back to 4.1% in the third quarter of 2009 as the Hong Kong economy was mired in recession. The figure declined in tandem with economic recovery taking hold afterwards. While the Hong Kong economy contracted year-on-year in the third quarter of 2019, the unemployment rate remained low. The proportion of low-income households (2.7%) was largely steady over a year earlier, still at a relatively low level in recent years (*Table 2 and Chart 1*).

(3) All figures pertaining to low-income households in the third quarter of 2019 are provisional figures.

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

<u>Period</u>	Household type:		<u>Total</u>	Of which:
	<u>Elderly households[#]</u>	<u>Non-elderly households</u>		<u>Economically active persons therein</u>
Q3 2003	3 000 (0.1)	113 400 (5.3)	116 500 (5.5)	140 600 [4.3]
Q3 2007	2 700 (0.1)	70 500 (3.1)	73 200 (3.2)	80 600 [2.4]
Q3 2008	2 700 (0.1)	79 100 (3.5)	81 700 (3.6)	91 200 [2.7]
Q3 2009	1 700 (0.1)	91 800 (4.0)	93 500 (4.1)	107 600 [3.1]
Q3 2011	3 800 (0.2)	55 600 (2.3)	59 300 (2.5)	66 000 [1.9]
Q3 2013	4 400 (0.2)	67 600 (2.8)	72 000 (3.0)	79 300 [2.2]
Q3 2015	3 900 (0.2)	56 200 (2.3)	60 100 (2.4)	67 400 [1.9]
Q3 2017	7 000 (0.3)	65 400 (2.6)	72 400 (2.8)	79 800 [2.2]
Q3 2018	6 400 (0.2)	62 700 (2.4)	69 100 (2.7)	76 200 [2.1]
Q3 2019	6 800 (0.3)	65 100 (2.5)	71 900 (2.7)	77 000 [2.1]

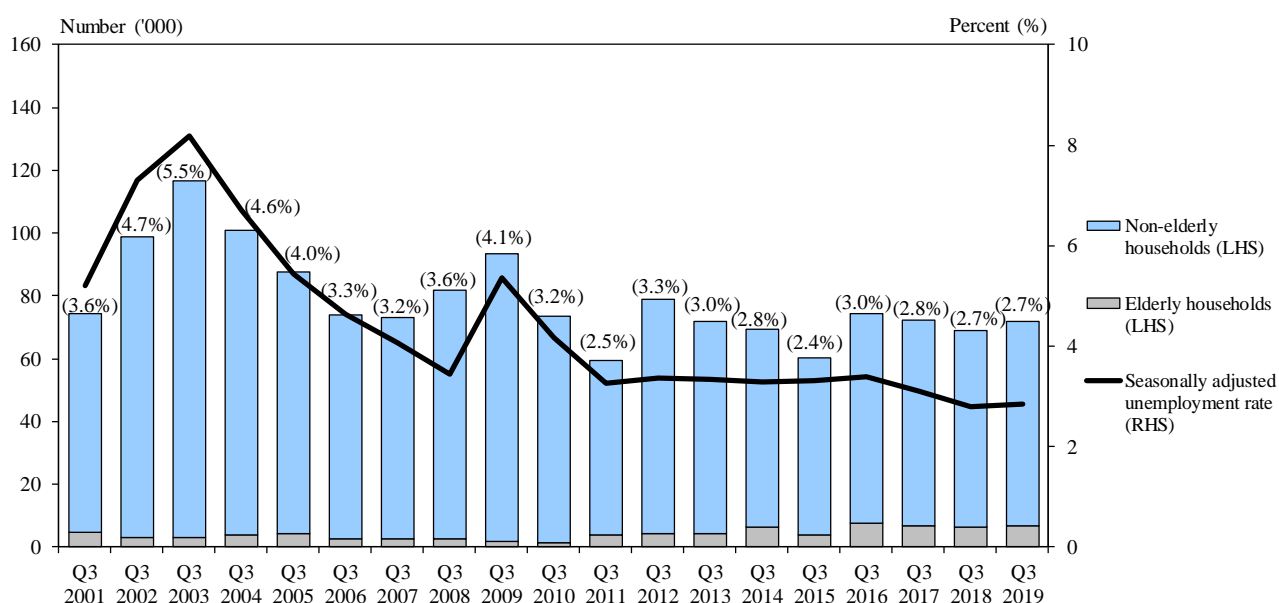
Notes : (*) Low-income households refer to households with monthly household income less than \$8,900 (Q3 2019 prices). This does not include households with all members being economically inactive.

(#) 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*



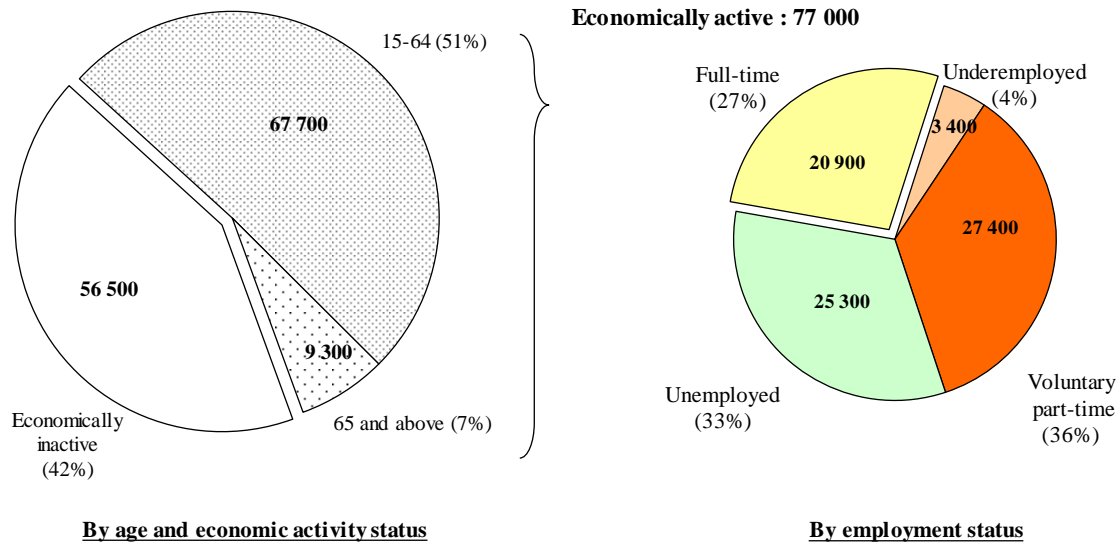
Notes : (*) Low-income households refer to households with monthly household income less than \$8,900 (Q3 2019 prices). This does not include households with all members being economically inactive. Figures in brackets are the proportions of low-income households in all domestic households.

Socio-economic characteristics of low-income households

6. Further decomposition of low-income households in the third quarter of 2019 reveals the following observations:

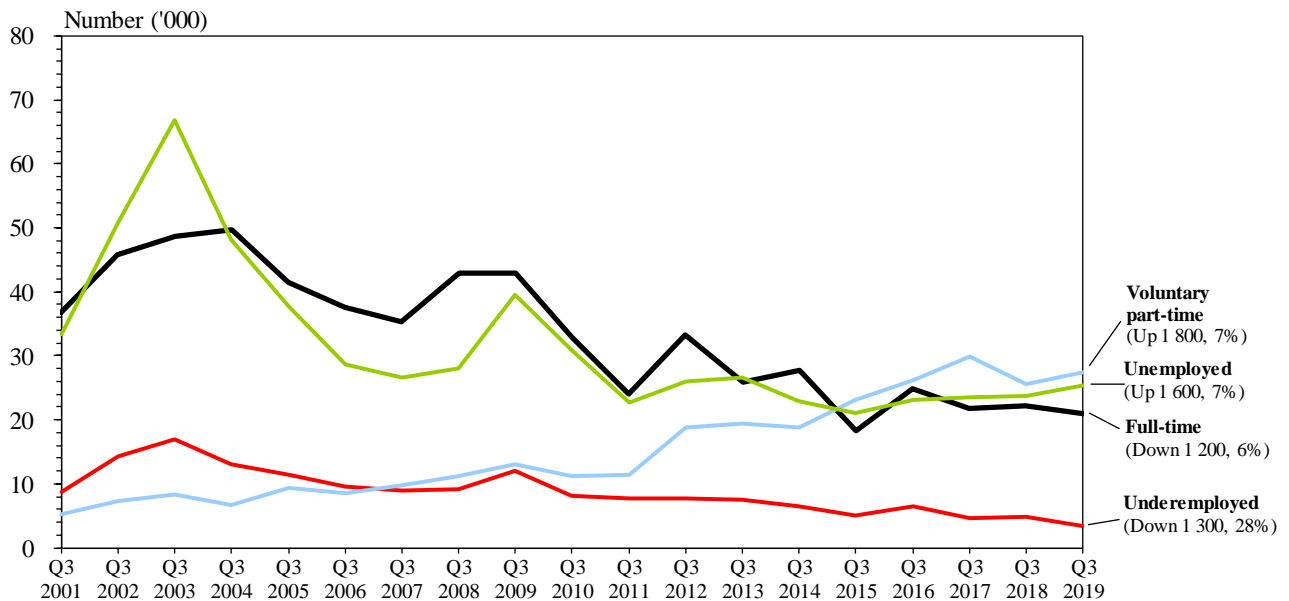
- There were 133 500 persons in the households in question, among whom 77 000 were economically active. Most of these economically active individuals (67 700 or 88%) were aged 15-64, with the majority within the age group of 40-64 (51 100 or 66%), whilst those aged 65 and above amounted to around one-tenth (9 300).
- The remaining 56 500 persons were economically inactive. 26 600 of them (47%) were either children aged below 15 or elderly persons aged 65 and above.
- Further analysis by employment status shows that among these 77 000 economically active persons, voluntary part-timers, unemployed and underemployed persons accounted for 36%, 33% and 4% respectively, while the proportion of full-time workers was only 27% (**Chart 2**). Among these, the number of voluntary part-timers and unemployed both rose by 7% over a year earlier (**Chart 3**).

Chart 2 : Persons living in low-income households* by age and economic activity status, Q3 2019



Note : (*) Low-income households refer to households with monthly household income less than \$8,900 (Q3 2019 prices). This does not include households with all members being economically inactive.

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



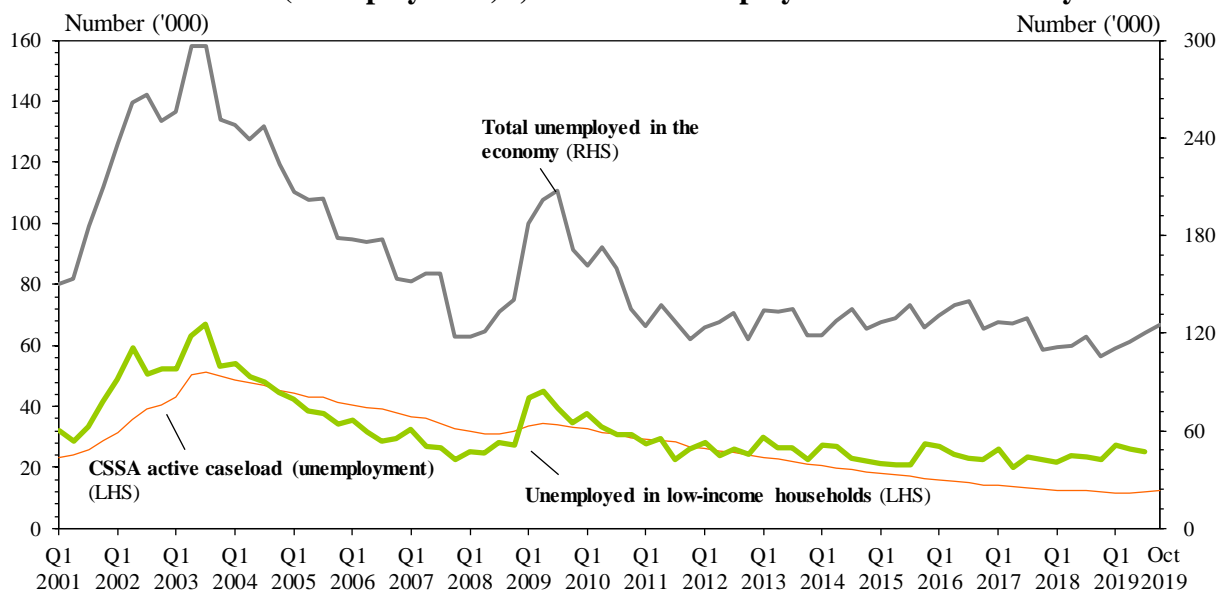
Notes : (*) Low-income households refer to households with monthly household income less than \$8,900 (Q3 2019 prices). This does not include households with all members being economically inactive. Figures in brackets are the year-on-year changes in number of economically active persons in Q3 2019.

- Analysed by occupation, the majority of the employed persons living in low-income households (78%) were lower-skilled workers (34% were elementary workers, and 24% 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 (14 700 or 29%), followed by transportation, storage, postal and courier services sector (4 600 or 9%).

The number of CSSA cases

7. The lower-skilled unemployment rate in August – October 2019 rose by 0.3 percentage point from a year earlier to 3.2%. As the labour market eased somewhat of late, the number of CSSA unemployment cases rose back to 12 282 in October by 572 (or 4.9%) from its low in June 2019, and also up by 80 (or 0.7%) when compared to a year earlier (*Chart 4*). As regards the number of overall CSSA caseload, the downward trend since late-2009 largely remained. It amounted to 220 775 cases in October 2019, still down in recent period. When compared on a year-on-year basis, the decline was 7 775 (or 3.4%).

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 \$8,900 (Q3 2019 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 adopt a multi-pronged approach to strengthen employment / training and retraining services so as to provide support to job-seekers and encourage self-reliance, 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 in a knowledge-based society, increase social mobility, and reduce the child poverty risk and inter-generational poverty. To improve the livelihood of the grassroots, one fundamental solution is to promote overall economic growth so as to provide more employment and income opportunities.

9. Amid the subdued local economic conditions, the labour market would unavoidably be affected. The Government has rolled out a series of relief measures, and the Chief Executive also announced in the Policy Address various new initiatives to alleviate poverty and support the disadvantaged. The Government will closely monitor the employment and incomes situation of grassroots workers and low-income households, and will provide measures as and when necessary.

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