

## Fifth Meeting of the Economic and Employment Council

### *Agenda Item 4 : Recent Situation of the Overall Economy and the Labour Market and Outlook for 2005*

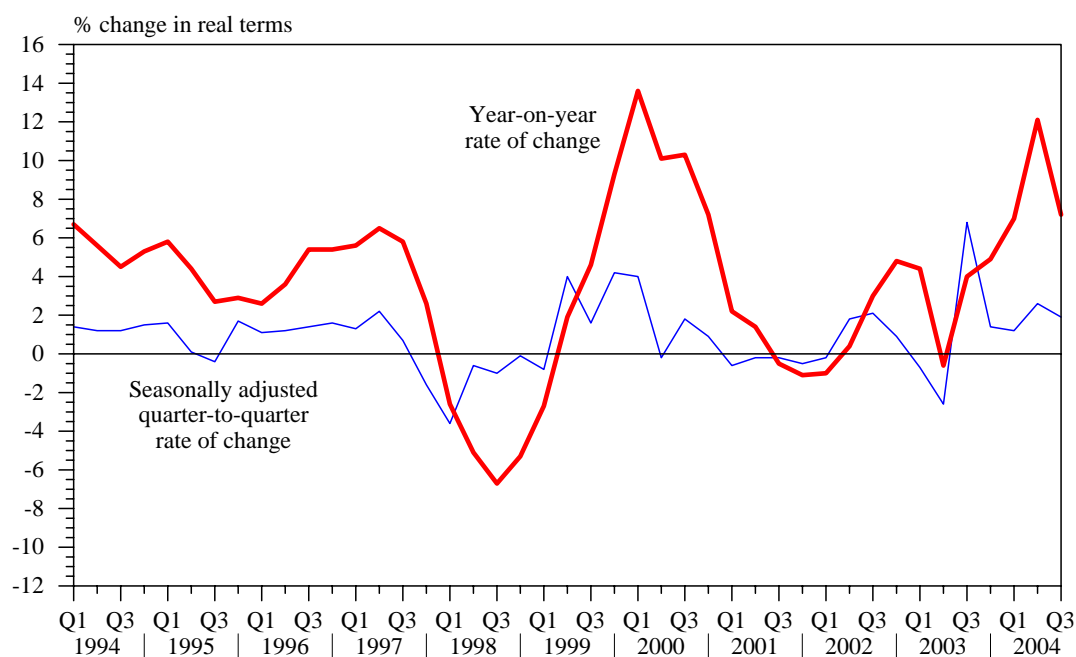
#### Introduction

This paper presents the recent developments in the local economy and the latest situation in the labour market. It concludes with a broad overview of the economic outlook for 2005.

#### Recent economic situation

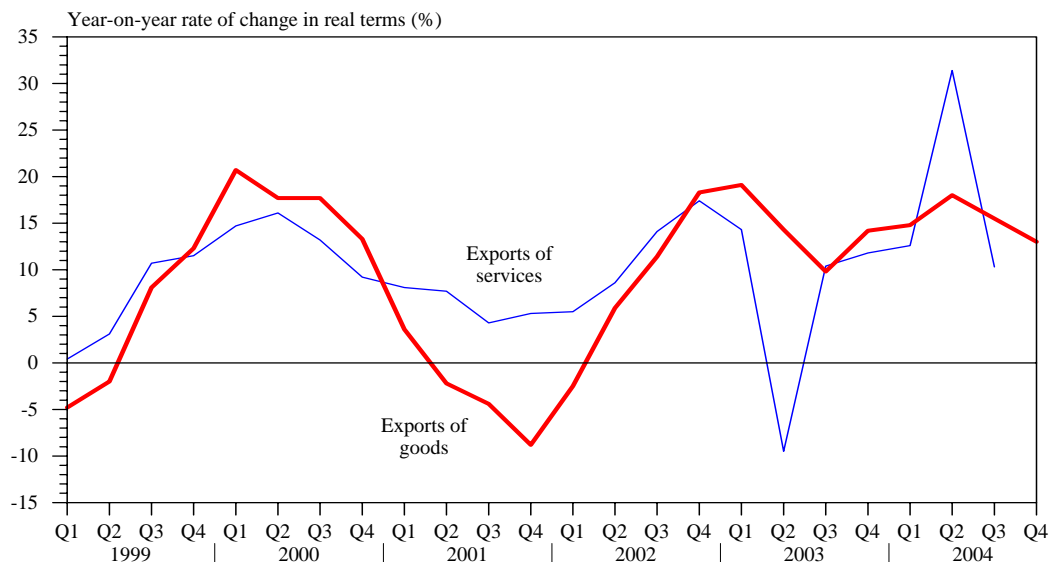
2. The upturn in the Hong Kong economy became more entrenched and full-fledged over the course of 2004, spurred by thriving merchandise exports and offshore trade, robust inbound tourism, and also vibrant consumer and investment spending. In the third quarter of 2004, the *Gross Domestic Product* (GDP) attained a further notable growth at 7.2% in real terms over a year earlier (*Chart 1*). Latest indications are that domestic and external demand remained buoyant in the fourth quarter of last year. For 2004 as a whole, the economy is likely to have grown by at least 7.5% in real terms, the fastest growth in four years.

**Chart 1 : Gross Domestic Product**



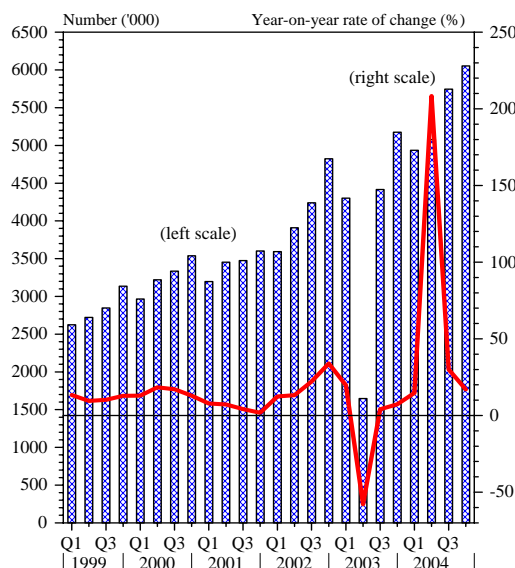
3. External trade continued to flourish in late 2004, as global demand stayed generally strong despite volatile movements in crude oil prices and US dollar, and as the Mainland economy sustained strong growth momentum. In the fourth quarter of 2004, *total exports of goods* registered double-digit growth for the tenth consecutive quarter, by around 13% in real terms over a year earlier. *Exports of services* were likewise robust, buoyed by vibrant inbound tourism and surging offshore trade (**Chart 2**). The number of visitor arrivals registered another robust double-digit growth of 17% in the fourth quarter over a year earlier, bringing the number of visitor arrivals to a record high of 21.8 million for 2004 as a whole (**Charts 3**).

**Chart 2 : Total exports of goods and exports of services**

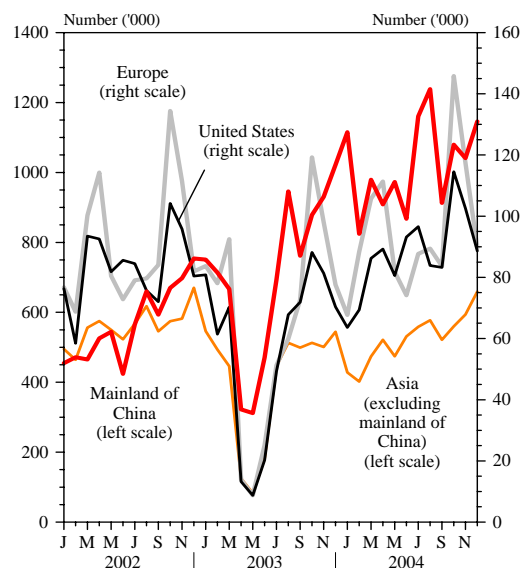


**Chart 3 : Visitor arrivals**

**(a) Overall level and growth**

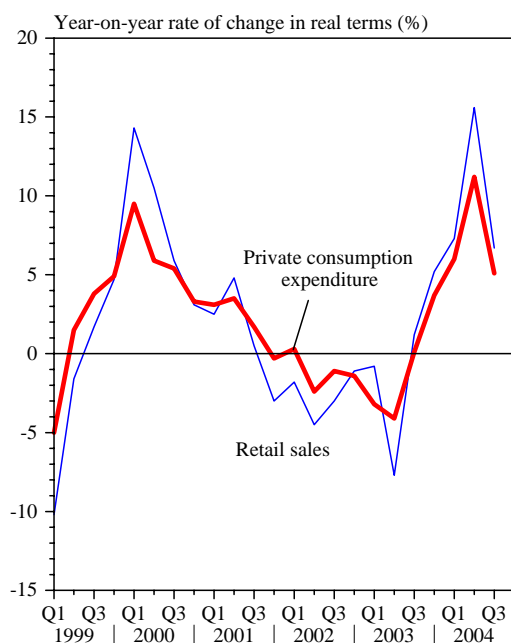


**(b) By source**

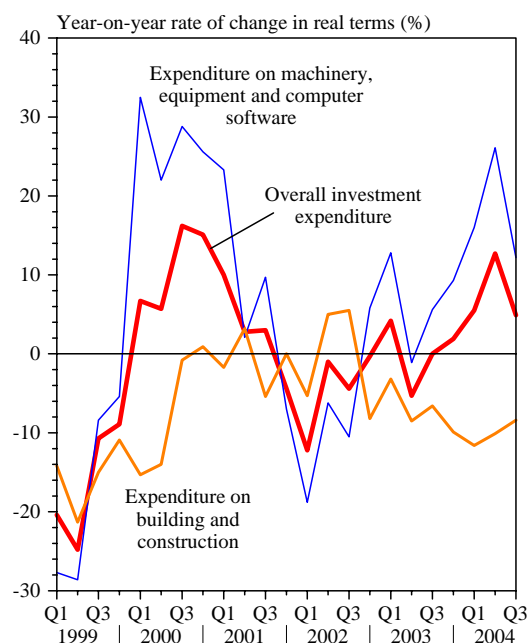


4. The domestic sector also picked up. Amidst sustained improvement in employment situation and generally buoyant performance of the asset markets, *private consumption expenditure* attained an average growth of 7% in real terms in the first three quarters of 2004 over a year earlier, contrasted against a 1% decline in 2003 (**Chart 4(a)**). Over the same period, *overall investment spending* leaped by 8% in real terms, primarily driven by double-digit surge in machinery and equipment investment, which in turn was buoyed by improved business sentiment after the launch of Closer Economic Partnership Arrangement (CEPA) and sustained growth in overall business activity. But the slack construction output was still holding back the upturn in investment (**Chart 4(b)**).

**Chart 4(a) : Private consumption expenditure and retail sales**

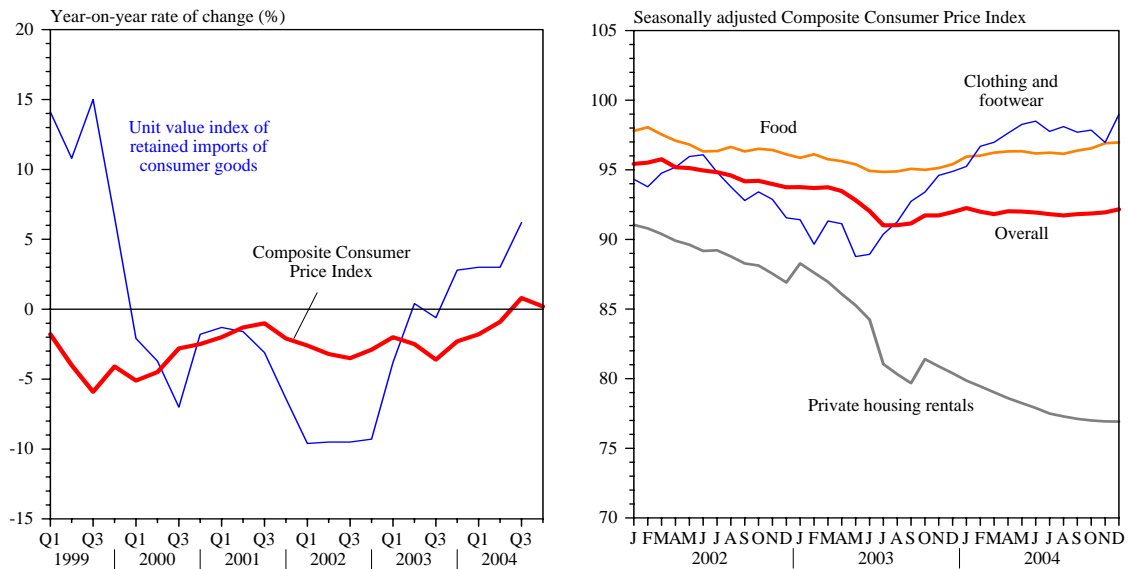


**Chart 4(b) : Investment expenditure by major component**



5. In July 2004, the 68-month long deflation finally gave way to inflation, a sign of return of pricing power to local retailers as retail business revived. Overall *consumer price inflation* was nevertheless still very modest up to the end of 2004, being kept down by earlier fall-off in housing rental. In December 2004, the Composite CPI data increased by just 0.2%, same as that in October and November. For 2004 as a whole, consumer prices fell by an average of 0.4%, after the 2.6% decrease in 2003 (**Chart 5**).

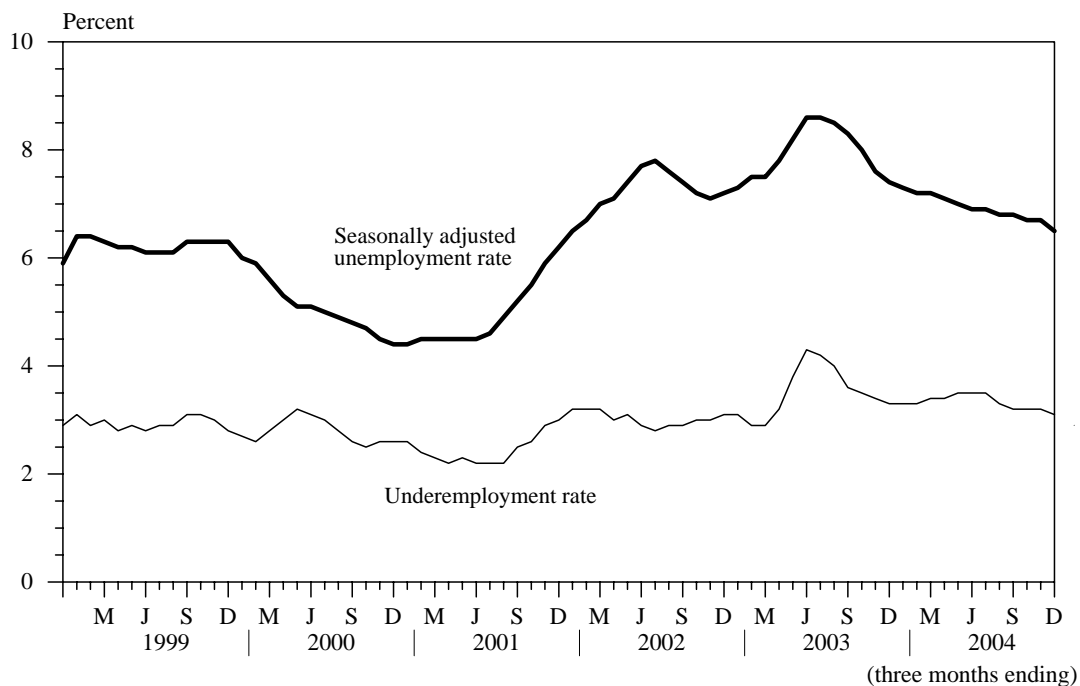
**Chart 5 : Hong Kong's price movement**



## Recent developments in the labour market

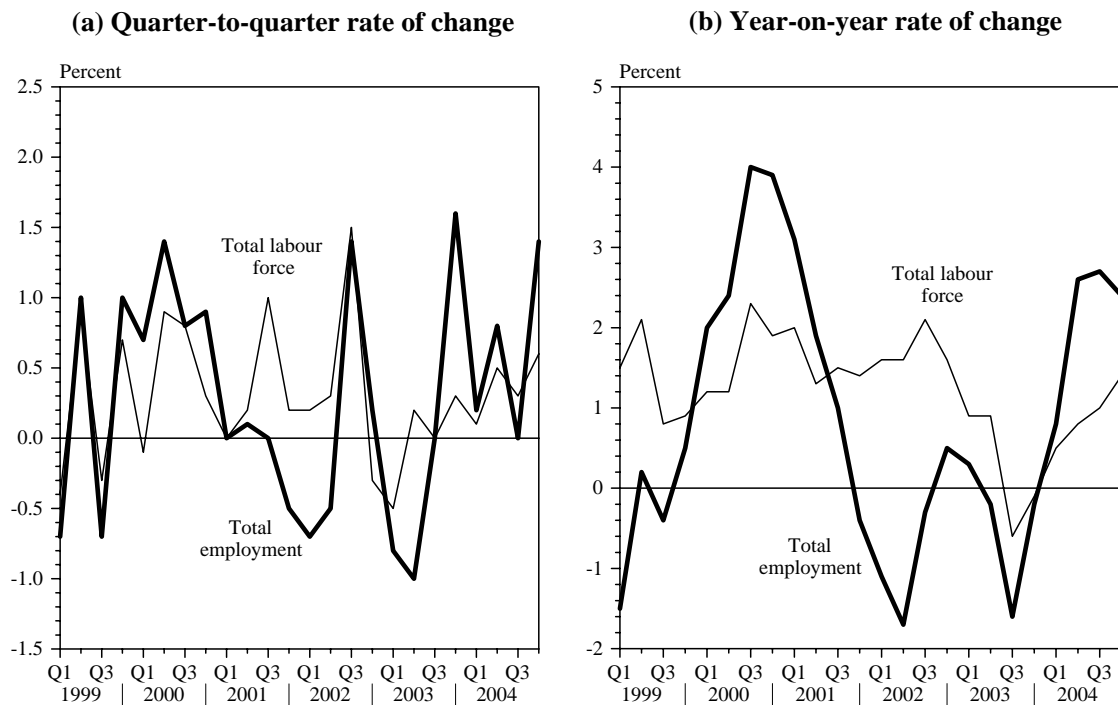
6. The labour market improved progressively over the course of 2004, as the economic growth gathered momentum and became more broad-based. In the fourth quarter of 2004, the *seasonally adjusted unemployment rate* fell to a 35-month low of 6.5%. In absolute terms, the total number of unemployed were reduced to 227 000 (*Chart 6*).

**Chart 6 : Unemployment and underemployment rates**



7. As labour demand strengthened along with the economic upturn, total employment expanded by 2.1% in 2004, the first increase in 3 years and the fastest since 2000 (**Chart 7**). At end-2004, total employment reached a new high of 3.33 million, which represented a visible gain of 138 900 or 4.3% from the trough in mid-2003.

**Chart 7 : Total labour force and total employment**



8. As another manifestation of improved labour demand, *vacancies* surged across many sectors. The number of vacancies received by the Labour Department went up by 40.4% in the fourth quarter of 2004 over a year earlier and by 34.6% for 2004 as a whole. Also, the number of placements achieved rose visibly, by 26.9% and 30.5% respectively. The downward pressure on *labour income* was also receding. In overall terms, labour earnings edged lower by only 0.5% year-on-year in money terms in the third quarter of 2004, whereas modest increases were observed in some of the economic sectors, including the wholesale and retail trades, restaurants and hotels, and water and air transport sectors.

## **Economic outlook for 2005**

9. The outlook for the Hong Kong economy for 2005 still hinges on the developments in the global economic environment, with volatile movements of crude oil prices as well as the US dollar posing the key external risks. Yet at this juncture, the widely held view is that the world economy should sustain solid growth momentum in 2005, although the pace of expansion is likely to come down from the exceptionally robust growth in 2004. Moreover, on the competitiveness front, a competitive and growing Mainland economy, both as a production hinterland and as a fast growing market, is Hong Kong's key advantage. Thus, granting a relatively stable external environment and with the implementation of the second phase of CEPA as from January 2005, there should still be good trading and business opportunities for Hong Kong.

10. As the property market has finally turned the corner, and as the economic upturn increasingly translates into an increase in employment opportunities, the recovery in the domestic sector is poised for further revival. Hence, economic growth this year is likely to be more balanced between external and domestic demand. Overall, it is believed that the Hong Kong economy would have another year of solid growth in 2005. The latest known forecasts from the major international organisations and local analysts for Hong Kong's economic growth in real terms for 2005 range from 4% to 6%, averaging at around 5%. On the price front, most analysts expect modest inflation in the range of 1% to 2.5%, averaging at around 1.5%.

11. In tandem with continued economic expansion, the labour market is likely to show further improvement in 2005. In particular, total employment is expected to remain on an uptrend, as the sustained pick-up in business activity would generate more job opportunities in the corporate sector. The opening of Hong Kong Disneyland in September this year, as well as further extension of the Individual Visit Scheme for Mainland residents coming to Hong Kong, should also add to labour demand in the tourism-related sectors. Yet, the prospect for further notable improvement in the labour market also hinges on structural factors, such as the on-going skill mismatch in the local workforce. Analysts in the private sector generally expect the unemployment rate to improve further in 2005. Their latest forecasts of the average unemployment rate for this year are in the range of 5.5 - 6.4%, averaging at around 6.0%.