

THIRD QUARTER ECONOMIC REPORT 2003

ECONOMIC ANALYSIS DIVISION
FINANCIAL SERVICES AND THE TREASURY BUREAU
GOVERNMENT OF THE
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CHAPTER 1 : OVERALL VIEW

Overall situation

1.1 After the setback caused by Severe Acute Respiratory Syndrome (SARS) in the second quarter, the Hong Kong economy rebounded distinctly to an appreciable growth in the third quarter of 2003. The turnaround was most conspicuous in the tourism-related sectors, driven by a sharp resurgence in visitor arrivals from the mainland of China (the Mainland), particularly so after the launch of the “individual visit” scheme in late July⁽¹⁾. Also, local consumer spending was steadily re-activated, resuming increase for the first time in two years, upon better sentiment and improving labour market conditions. As to investment spending, building and construction output was still slack in overall terms. Yet machinery and equipment acquisition picked up visibly, albeit supported in part by intake of some aircraft ordered earlier.

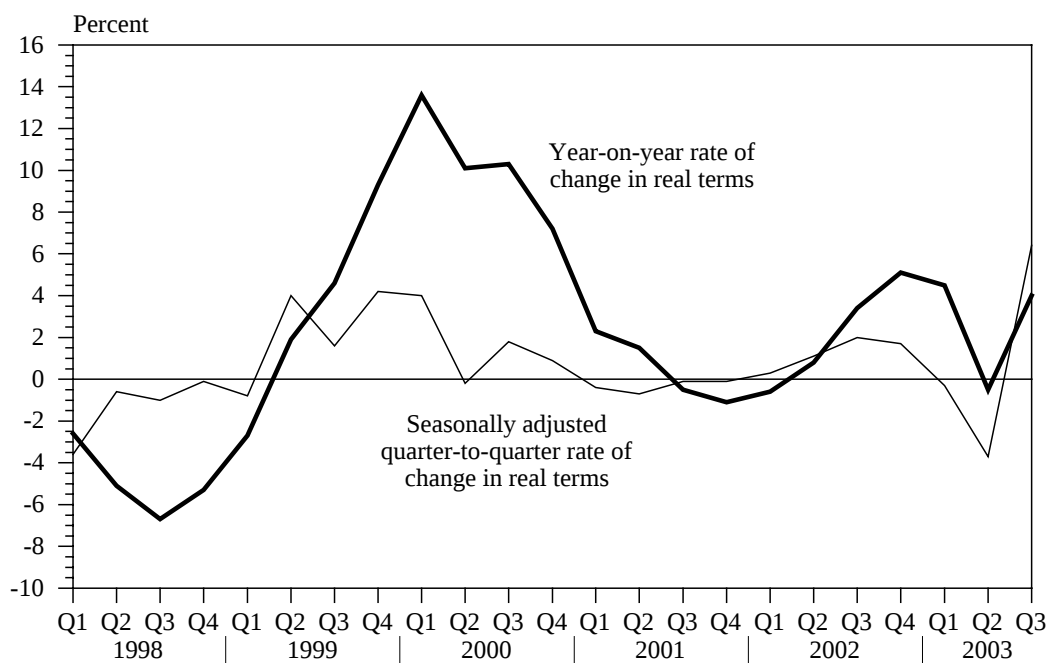
1.2 Externally, total exports of goods remained generally robust in the third quarter of 2003, even though the growth pace was not as marked as in the earlier months due in part to shifting to a higher base of comparison. Exports to the United States continued on a decline. But exports to the European Union held up well. Moreover, exports to many of the East Asian markets sustained growth approaching or exceeding 20%. Concurrently, offshore trade remained buoyant, along with the surging external trade in the Mainland.

1.3 In the third quarter of 2003, the *Gross Domestic Product (GDP)*⁽²⁾ rebounded distinctly to growth at 4.0% in real terms over a year earlier, in contrast to a 0.5% decline in the second quarter (latter figure unchanged from the estimate put out earlier). On a seasonally adjusted quarter-to-quarter comparison⁽³⁾, the turnaround in GDP was even more pronounced, with a 6.4% leap in real terms in the third quarter of 2003, as against a 3.7% dip in the second quarter (latter figure also unchanged from the estimate put out earlier).

/Diagram 1.1

Diagram 1.1

Gross Domestic Product



/Table 1.1

Table 1.1

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

	<u>2001[#]</u>	<u>2002[#]</u>	<u>Q1[#]</u>	<u>2002</u>			<u>Q1[#]</u>	<u>2003</u>	
<i>Change in real terms of GDP and its main expenditure components (%)</i>				<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>		<u>Q2[#]</u>	<u>Q3⁺</u>
Private consumption expenditure ^(^)	2.0	-1.2	-0.1	-2.4	-0.9	-1.3	-1.7	-2.6	2.0
Government consumption expenditure	6.1	2.4	2.3	3.0	3.5	0.8	1.3	0.4	0.5
Gross domestic fixed capital formation	2.7	-4.3	-11.8	-0.2	-4.3	-0.7	3.5	-5.7	-0.4
of which :									
Building and construction	-1.1	1.2	-3.2	7.6	8.2	-6.2	-3.5	-8.4	-6.4
Machinery, equipment and computer software	6.2	-9.1	-19.8	-6.7	-12.2	3.2	11.9	-2.0	4.9
Total exports of goods	-3.3	8.7	-2.4	5.9	11.5	18.4	19.1	14.3	10.0
Re-exports	-2.4	11.0	-1.4	8.4	13.7	22.2	22.3	17.0	11.5
Domestic exports	-10.2	-11.2	-11.1	-13.6	-7.5	-12.9	-12.0	-12.6	-5.2
Imports of goods ^(a)	-1.9	7.9	-4.0	6.0	10.8	18.2	18.8	10.9	8.2
Exports of services ^(^)	6.2	12.2	6.3	9.1	14.0	18.1	12.5	-13.9	6.9
Imports of services	2.0	0.2	-0.7	-3.8	2.0	3.4	-3.9	-19.6	0.5
Gross Domestic Product	0.5	2.3	-0.6	0.8	3.4	5.1	4.5	-0.5	4.0
<i>Change in the main price indicators (%)</i>									
GDP deflator	-1.9	-3.0	-2.3	-2.2	-3.1	-4.1	-4.6	-5.4	-5.7
Composite Consumer Price Index^(b)	-1.6	-3.0	-2.6	-3.2	-3.5	-2.9	-2.0	-2.5	-3.6
Consumer Price Index (A) ^(b)	-1.7	-3.2	-2.8	-3.6	-4.1	-2.4	-1.8	-1.8	-3.3
<u>Change in nominal GDP (%)</u>	-1.4	-0.8	-3.0	-1.4	0.2	0.8	-0.2	-5.9	-1.9
<u>GDP at current market prices (\$ billion)</u>	1,270	1,260	298	306	325	331	298	288	318
<u>GDP at constant (2000) market prices (\$ billion)</u>	1,294	1,324	310	318	343	353	324	316	357
<u>Changes in inventories at constant (2000) market prices (\$ billion)</u>	-5	3	-3	1	1	3	3	2	-2

Notes : (#) Revised figures.

(+) Preliminary figures.

(^) Revised series incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003. For details, see Box 1.1.

(a) Here imports of goods are valued on f.o.b. basis, instead of on c.i.f. basis as is the on-going practice for the merchandise trade statistics.

(b) Final figures.

/Table 1.2

Table 1.2

**Gross Domestic Product and its main expenditure components
and the main price indicators
(seasonally adjusted quarter-to-quarter rate of change (%))**

	<u>2002</u>				<u>2003</u>		
	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3⁺</u>
<i>Change in real terms of GDP and its main expenditure components (%)</i>							
Private consumption expenditure ^(^)	0.4	-0.9	-0.1	-0.4	-0.6	-1.3	4.6
Government consumption expenditure	0.4	-0.2	2.3	-1.2	0.1	-0.3	1.8
Gross domestic fixed capital formation	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Total exports of goods	4.6	5.7	4.1	3.9	3.1	2.4	0.2
Re-exports	5.8	6.6	4.6	4.7	3.9	2.7	-0.4
Domestic exports	-5.5	-2.0	-0.6	-4.3	-6.3	-1.8	8.5
Imports of goods ^(a)	4.6	5.9	4.6	3.0	3.7	-0.9	2.0
Exports of services ^(^)	2.5	4.8	5.9	4.1	-2.6	-20.0	31.0
Imports of services	0.4	-1.6	3.8	1.1	-6.9	-17.7	29.7
Gross Domestic Product^(b)	0.3	1.1	2.0	1.7	-0.3	-3.7	6.4
<i>Change in the main price indicators (%)</i>							
GDP deflator	-0.7	-0.8	-0.9	-1.6	-1.4	-1.6	-1.2
Composite Consumer Price Index^(c)	-1.1	-0.6	-0.7	-0.6	-0.1	-1.1	-1.9
Consumer Price Index (A) ^(c)	-0.6	-0.6	-0.7	-0.6	*	-0.5	-2.3

Notes : (#) Revised figures.

(+) Preliminary figures.

(^) Revised series incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003. For details, see Box 1.1.

(*) Change of less than 0.05%.

N.A. Not applicable, as no clear seasonal pattern is found in gross domestic fixed capital formation, due to the presence of considerable short-term fluctuations.

(a) Here imports of goods are valued on f.o.b. basis, instead of on c.i.f. basis as is the on-going practice for the merchandise trade statistics.

(b) As gross domestic fixed capital formation does not exhibit a clear seasonal pattern, the seasonally adjusted series of GDP is compiled separately at the overall level.

(c) Final figures.

/1.4

1.4 Prompted by the upturn in economic activity, *labour market* conditions were also set to improve. The seasonally adjusted unemployment rate fell to 8.3% in the third quarter of 2003, from 8.6% in the second quarter. Lesser unemployment was seen mostly in the earlier SARS affected sectors. The underemployment rate came down more visibly, from 4.3% to 3.6%, as many of the employees having been suspended earlier resumed work in the more recent months. Yet labour earnings and wages were still soft.

1.5 The *property market* turned more active in the third quarter of 2003, as sentiment was rekindled by better performance in the economy and rally in the local stock market. On residential property, transactions in the primary market picked up visibly. In turn, trading in the secondary market was also bolstered. The trend of decline in flat prices appeared to have been arrested towards the end of the third quarter. On commercial property, there was some pick-up in market activity, notably for retail premises in prime locations. For office space, rentals were still soft, yet prices seemed to have stabilised somewhat. For shopping space, prices and rentals in the popular areas had firmed. As to industrial property, the market stayed sluggish in overall terms.

1.6 In the *financial market*, the spot exchange rate of the Hong Kong dollar against the US dollar strengthened during the third quarter of 2003, and the spread of the twelve-month Hong Kong dollar forward rate against the spot rate switched from a premium to a discount towards the end of the quarter. There was an increased demand for Hong Kong dollar assets, induced by optimism about the improved performance and near-term outlook of the Hong Kong economy as well as by the weakening of the US dollar against currencies in the region. As liquidity in the banking sector went higher along with increased inflow of funds, the negative spread of the three-month HIBOR against the corresponding Euro-dollar deposit rate widened. With Hong Kong dollar loans contracting further whereas with Hong Kong dollar deposits expanding further, the respective loan-to-deposit ratio went down appreciably further. The local stock market was on a general uptrend during the third quarter, boosted variously by signing of the Closer Economic Partnership Arrangement (CEPA) between Hong Kong and the Mainland⁽⁴⁾, launch of the “individual visit” scheme for Mainland visitors to Hong Kong, increased inflow of funds, and general uptrend in the overseas stock markets. The Hang Seng Index surged to a high of 11 296 on

/24 September.....

24 September, and closed the month at 11 230, 17.3% above the level at end-June. Transactions were hectic, with the average daily turnover leaping to \$12.0 billion in the third quarter, from \$8.1 billion in the second quarter.

1.7 On *consumer prices*, the Composite Consumer Price Index had a larger decline, by 3.6% in the third quarter of 2003 over a year earlier, as against 2.5% in the second quarter. But this was mostly due to the rates concession and the waiver of water and sewage charges granted as relief measures by the Government, which had the combined effect of dampening the Composite CPI by about one percentage point in the third quarter. In fact, as economic activity progressively improved, the year-on-year rate of decline in the Composite CPI had been lessening, from 4.0% in July to 3.8% in August, and visibly further to 3.2% in September. This reversed the enlarging decline seen in the earlier months owing to the impact of SARS.

1.8 Statistics on the *Gross National Product (GNP)*⁽⁵⁾ are available up to the second quarter of 2003. Both external factor income inflow and outflow continued to decrease in the second quarter of 2003 over a year earlier. This was largely caused by further fall-off in interest income into and out of Hong Kong amidst a low interest rate environment globally. Balancing these flows, there was still a net inflow of external factor income amounting to 0.5% of GDP in the second quarter of 2003. With these flows decreasing to a broadly similar degree, GNP fell by 0.6% in real terms in the second quarter of 2003 over a year earlier, broadly comparable to the corresponding decline in GDP by 0.5% in real terms.

1.9 More specifically on external factor income, net direct investment income outflow decreased in the second quarter of 2003 over a year earlier, mainly due to a more substantial reduction in investment earnings by foreign enterprises in Hong Kong. Yet concurrently, net portfolio investment income inflow declined, largely on account of increased dividend pay-outs by resident companies to foreign investors more than offsetting increased pay-ins to resident investors from holding of foreign securities. Meanwhile, net income inflow on other investment also fell, along with larger reduction in interest income from loans and deposits placed abroad by local banks.

/Table 1.3

Table 1.3**Gross National Product and external factor income flows**

	<u>2001</u>	<u>2002</u>	<u>2002</u>				<u>2003</u>	
			<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
<i>Year-on-year rate of change in money terms (%)</i>								
Total external factor income flow ^(a)								
Inflow	-7.7	-15.7	-17.0	-28.4	-9.5	-4.2	-1.5	-3.0
Outflow	-13.1	-13.6	-21.1	-26.8	-3.0	2.2	-3.5	-2.3
Net external factor income flow at current market prices (\$ billion)	41	27	15	2	8	2	16	2
GDP at current market prices (\$ billion)	1,270 (-1.4)	1,260 (-0.8)	298 (-3.0)	306 (-1.4)	325 (0.2)	331 (0.8)	298 (-0.2)	288 (-5.9)
GNP at current market prices (\$ billion) ^(b)	1,311 (0.1)	1,287 (-1.8)	313 (-2.5)	308 (-2.4)	333 (-1.8)	333 (-0.7)	314 (0.2)	290 (-6.1)
<i>Year-on-year rate of change in real terms (%)</i>								
Gross National Product	2.0	1.2	-0.1	-0.2	1.3	3.6	4.9	-0.6

Notes : (a) External factor income comprises direct investment income, portfolio investment income, other investment income, and compensation of employees.

(b) GNP is equal to GDP plus net external factor income flow.

() Figures in brackets represent the year-on-year rates of change in money terms in GDP and GNP respectively.

The external sector

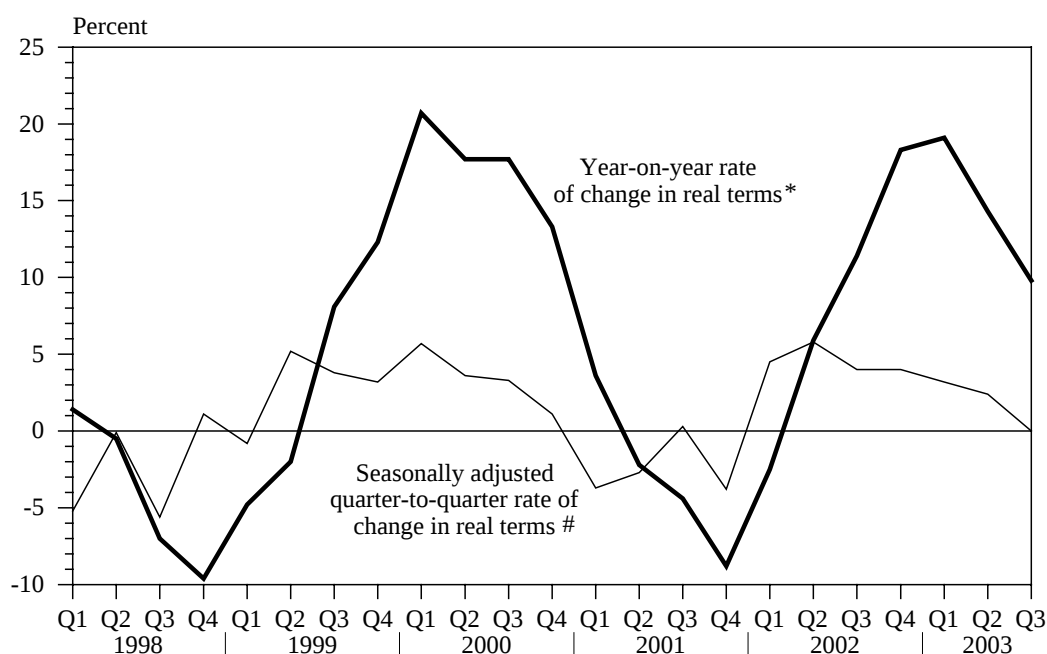
1.10 Hong Kong's merchandise exports continued to show notable growth in the third quarter of 2003, amidst generally improved global and regional economic environment and with the earlier weakening in the US dollar still giving some positive boost. But the growth pace was not as marked as in the first half of the year, due in part to a higher base of comparison in the third quarter of 2002. According to the merchandise trade statistics, *total exports of goods* (comprising re-exports and domestic exports) grew by 9.8% in real terms in the third quarter of 2003 over a year earlier. On the monthly profile, export growth in

/real

real terms was 10.4% in July, 9.8% in August and 9.3% in September. The effect of a higher base of comparison was more appreciable in September, as exports accelerated to a double-digit increase in September last year. Together with a 16.5% surge in the first half of the year, total exports of goods leaped by 13.9% in real terms in the first nine months of 2003 over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, total exports of goods were virtually unchanged in real terms in the third quarter of 2003, after rising for six consecutive quarters and up by 3.2% in the first quarter and 2.4% in the second quarter (paragraph 2.7).

Diagram 1.2

Total exports of goods



- Notes : (*) From the first quarter of 2001 onwards, the rates of change are computed from the new 2000-based trade index series. Before then, the rates of change are computed from the old 1990-based series. Re-scaling using conversion factors as derived from the levels of the old and the new series in their overlapping period of 2000 has been applied to the indices to maintain continuity.
- (#) From the second quarter of 2000 onwards, the rates of change are computed from the new 2000-based trade index series. Before then, the rates of change are computed from the old 1990-based series. Re-scaling using conversion factors as derived from the levels of the old and the new series in their overlapping period of 2000 has been applied to the indices to maintain continuity.

/1.11

1.11 *Re-exports* remained the key driver of growth within total exports of goods, leaping by 11.3% in real terms in the third quarter of 2003 over a year earlier. There were double-digit increases in real terms for each month of the third quarter, at 12.2%, 11.0% and 10.7% respectively. For the first nine months of 2003 taken together, re-exports soared by 16.3% in real terms over a year earlier, having increased distinctly by 19.4% in the first half of the year. On a seasonally adjusted quarter-to-quarter comparison, re-exports however fell back modestly, by 0.6% in real terms in the third quarter of 2003, having risen by 4.0% and 2.7% respectively in the first and second quarters. *Domestic exports* continued to be suppressed by the on-going structural shift towards re-exports and offshore trade. In the third quarter of 2003, domestic exports fell further, by 5.4% in real terms over a year earlier. As to the individual months in the third quarter, the declines in real terms were 7.3%, 2.8% and 6.0% respectively. Along with a 12.3% slump in the first half of the year, domestic exports were down by 9.8% in real terms in the first nine months of 2003 over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, domestic exports nevertheless reverted to increase, up distinctly by 8.2% in real terms in the third quarter of 2003, after declines by 6.3% and 1.8% respectively in the first and second quarters (paragraphs 2.8 and 2.9).

1.12 Exports to the region remained the key driving force for Hong Kong's export growth. Total exports of goods to *East Asia* as a whole continued to be strong, rising by 17.9% in real terms in the third quarter of 2003 over a year earlier. Amongst the major markets, exports to the Mainland, the Republic of Korea, Singapore and Taiwan had growth approaching or exceeding 20% in real terms in the third quarter over a year earlier. Exports to Japan, Thailand and Indonesia also maintained double-digit growth. On the other hand, exports to Malaysia and the Philippines slipped into decline. Total exports of goods to *North America* slackened further, declining by 6.3% in real terms in the third quarter of 2003 over a year earlier. This went along with the deceleration in US import demand in that quarter. Conceivably also mattered was the further structural shift in re-exports to offshore trade for shipment to the US market. Total exports of goods to the *European Union* held up well, with a 10.6% rise in real terms in the third quarter of 2003 over a year earlier. The growth was largely attributable to enhanced price attractiveness of Hong Kong's exports brought about by the strength of the euro (paragraphs 2.17 to 2.19).

/1.13

1.13 *Imports of goods* grew further, by 7.9% in real terms over a year earlier in the third quarter of 2003 over a year earlier. The moderation from the double-digit growth in the preceding four quarters was mainly due to the slow-down in re-export growth from the highly hectic pace in the first half of this year. Also relevant was the continued weakness in imports for local use in most of the third quarter. But as such imports picked up, total imports also rose faster, by 9.2% in real terms in September, as against 7.3% in both July and August. Together with a 14.3% surge in the first half of the year, imports of goods rose by 11.9% in real terms in the first nine months of 2003 over a year earlier. Within total imports, *retained imports* rose back marginally by 0.6% in real terms in the third quarter of 2003 over a year earlier. Such imports were still weak in July and August, down by 2.8% and 0.9% respectively in real terms. A notable rebound to a 5.7% increase occurred in September, as local demand improved. Together with a 4.3% rise in the first half of the year, retained imports went up by 2.9% in real terms in the first nine months of 2003 over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, imports of goods rose back, by 2.2% in real terms in the third quarter of 2003, after a 3.6% increase in the first quarter and a 1.1% decline in the second quarter. Retained imports bounced up more strongly, by 9.3% in real terms in the third quarter of 2003, having risen by 2.9% in the first quarter and plunged by 9.6% in the second quarter (paragraph 2.10).

1.14 With the value of total exports of goods increasing faster than the value of imports of goods, the *visible trade deficit* reckoned on a GDP basis narrowed further, to \$1.4 billion or 0.3% of the value of imports of goods in the third quarter of 2003, from \$5.0 billion or 1.1% in the same quarter in 2002. For the first nine months of 2003 taken together, the visible trade deficit also narrowed, to \$27.2 billion or 2.1% of the value of imports of goods, from \$33.8 billion or 2.9% in the same period in 2002 (paragraph 2.11).

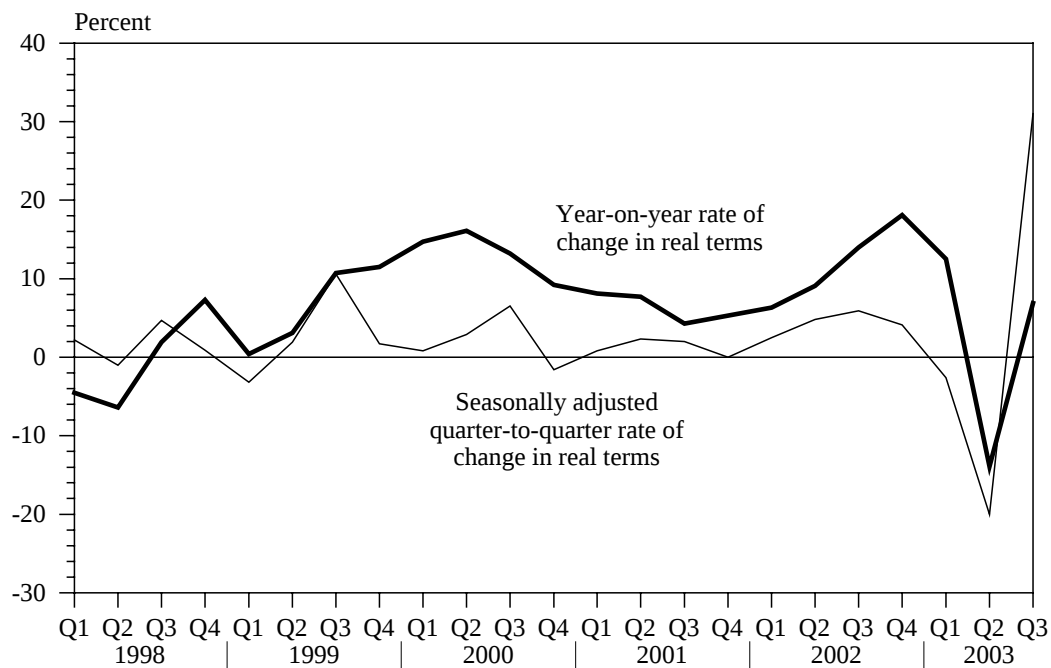
1.15 On invisible trade, *exports of services*, having plummeted sharply during the second quarter upon the impact of SARS, turned up visibly during the third quarter upon the swift revival in inbound tourism and continued buoyant offshore trade. In the third quarter of 2003, exports of services rose back by 6.9% in real terms over a year earlier, representing a sharp turnaround from the 13.9% plunge in the second quarter. Together with a 1.0% decline in the first half of the year, there was a 1.9% increase in real terms for the first three quarters of 2003

/as

as a whole over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, exports of services had a much more pronounced surge, by 31.0% in real terms in the third quarter of 2003, having fallen by 2.6% and 20.0% respectively in the first and second quarters (paragraph 2.12).

Diagram 1.3

Exports of services



/Box 1.1

Box 1.1**New tourism expenditure data and its effect
on the GDP statistics**

As a continuing effort to improve the quality of tourism statistics, the Hong Kong Tourism Board (HKTb) has undertaken a review of the statistical framework and revamped the data collection system. As a result of this review, HKTb's Departing Visitors Survey has been enhanced with a considerable increase in sample size. Data coverage is now more comprehensive than before, particularly in regard to the expenditure profile of same-day in-town visitors whose arrival has been growing very rapidly in recent years.

In line with the recommendations for tourism statistics stipulated by the World Tourism Organisation, HKTb will replace the previous set of data on "tourism receipts" by a more comprehensive set of data entitled "tourism expenditure associated to inbound tourism". The new set of tourism expenditure data comprises the following two main components :

- (1) *Destination consumption expenditure of incoming visitors and travellers*, which includes the expenditure in Hong Kong by overnight visitors, same-day in-town visitors, servicemen, aircrew members, transit/transfer passengers, and cruise passengers.
- (2) *Passenger international transportation expenditure*, which are the receipts of Hong Kong-based carriers for international transportation of non-resident visitors by air, sea or land.

Compared with the previous set of data, the coverage of tourism expenditure in the new set of data is expanded to include expenditure of cruise passengers and expenditure by passengers in international transportation. Furthermore, the estimation of destination consumption expenditure of incoming visitors and travellers is refined with separate constituent estimates for overnight visitors and same-day in-town visitors.

With the present enhanced framework, total tourism expenditure is estimated at \$77.4 billion in 2002, comprising \$58.5 billion in destination consumption expenditure of incoming visitors and travellers and \$18.9 billion in passenger international transportation expenditure. The total tourism expenditure rose by 25.3% in value terms over 2001.

The refinement made to the data on destination consumption expenditure of incoming visitors and travellers does not lead to any change in the overall Gross Domestic Product (GDP), as it affects the estimates on two of its expenditure components, viz. exports of services (XS) and private consumption expenditure (PCE), to the same absolute magnitude yet in the opposite direction, with XS down and PCE up.

As to the growth rate in real terms, that of PCE is revised from 1.6% and -1.3% in 2001 and 2002 to 2.0% and -1.2% respectively, while that of XS is revised from 6.9% and 11.7% to 6.2% and 12.2% respectively.

The incorporation of passenger international transportation expenditure does not affect the estimation of XS, as it is already included under the transportation item within XS, and hence also does not lead to any change in the overall GDP.

/1.16

1.16 *Imports of services* also recovered from the plunge brought about by SARS. There was a 0.5% rise in real terms in the third quarter of 2003 over a year earlier. The sharp turnaround from the 19.6% slump in the second quarter was underpinned by a swift revival in outbound travel and related transportation services. But with an 11.5% dip in the first half of the year, imports of services still fell markedly by 7.3% in real terms for the first three quarters of 2003 as a whole over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, imports of services had an even stronger rebound, rising by 29.7% in real terms in the third quarter of 2003, following decreases of 6.9% and 17.7% respectively in the first and second quarters (paragraph 2.13).

1.17 Taking exports and imports of services together, the *invisible trade surplus* reckoned on a GDP basis rose back to \$41.6 billion or 78.5% of the value of imports of services in the third quarter of 2003, from \$38.4 billion or 73.7% in the same quarter in 2002. For the first three quarters of 2003 as a whole, the invisible trade surplus also enlarged, to \$105.6 billion or 77.1% of the value of imports of services, from \$98.2 billion or 67.8% in the same period in 2002 (paragraph 2.14).

1.18 As the visible trade deficit narrowed while the invisible trade surplus expanded, the *combined surplus* reckoned on a GDP basis surged markedly, to \$40.2 billion or 7.7% of the total value of imports of goods and services in the third quarter of 2003, from \$33.4 billion or 6.8% in the same quarter in 2002. For the first three quarters of 2003 as a whole, the combined surplus went up to \$78.4 billion or 5.5% of the total value of imports of goods and services, as compared to \$64.4 billion or 4.9% in the same period in 2002 (paragraph 2.15).

Domestic demand

1.19 Local consumer spending revived steadily during the third quarter of 2003, as sentiment and labour market conditions both turned better. Coupling this with a strong upturn in inbound tourism, the volume of *retail sales* bottomed out, with the year-on-year change turning from a decrease of 0.3% in July to increases of 3.0% in August and 0.8% in September. The smaller increase in September than in August was attributable to the sales of festive food items being affected by the timing of the Mid-Autumn Festival, which occurred shortly before mid-September this year but in the latter part of September last year. For the third quarter of 2003 as a whole, the volume of retail sales went up modestly,

/by

by 1.2% over a year earlier, yet this already represented a distinct upturn from the 7.7% dip in the second quarter. While the improvement in retail sales was rather broad-based, there was particularly large increase in sales of such consumer durables as electrical goods and photographic equipment, and also furniture. On a seasonally adjusted quarter-to-quarter comparison, the volume of retail sales bounced up by 8.3% in the third quarter of 2003, having plummeted by 7.5% in the second quarter.

1.20 *Private consumption expenditure (PCE)* rebounded to increase, up by 2.0% in real terms in the third quarter of 2003 over a year earlier, having been down by 2.6% in the second quarter. This was the first increase in two years. The rebound was marked by almost across-the-board increases in spending on goods and services. Residents' spending abroad also showed a distinct relative improvement as people progressively resumed their outbound trips. On a seasonally adjusted quarter-to-quarter comparison, PCE rose visibly by 4.6% in real terms in the third quarter of 2003, reversing the 1.3% decrease in the second quarter.

/Table 1.4

Table 1.4

**Local consumer and visitor spending in the domestic market
(year-on-year rate of change in real terms (%))**

		<u>Retail sales</u> ^(a)	<u>Consumer spending by major component</u> ^(a)						<u>Visitor spending</u> ^(b)
			<u>Food</u>	<u>Durables</u>	<u>Non-durables</u>	<u>Services</u>	<u>Residents' expenditure abroad</u>	<u>Total</u>	
2002	Annual	-2.6	*	*	-5	3	-2	*	27
	Q1	-1.8 (2.1)	1	*	-2	2	-3	1	10
	Q2	-4.5 (-1.5)	*	-4	-8	3	-5	-1	26
	Q3	-3.0 (-1.4)	-1	*	-7	4	*	1	28
	Q4	-1.1 (0.1)	*	5	-4	3	-1	1	41
2003	Q1	-0.8 (1.0)	1	5	-5	1	-8	*	19
	Q2	-7.7 (-7.5)	*	-1	-17	-4	-29	-8	-71
	Q3	1.2 (8.3)	*	6	1	3	-1	2	4

Notes : (a) Retail sales and consumer spending by major component include both local consumer and visitor spending, which are not separable from the survey data.

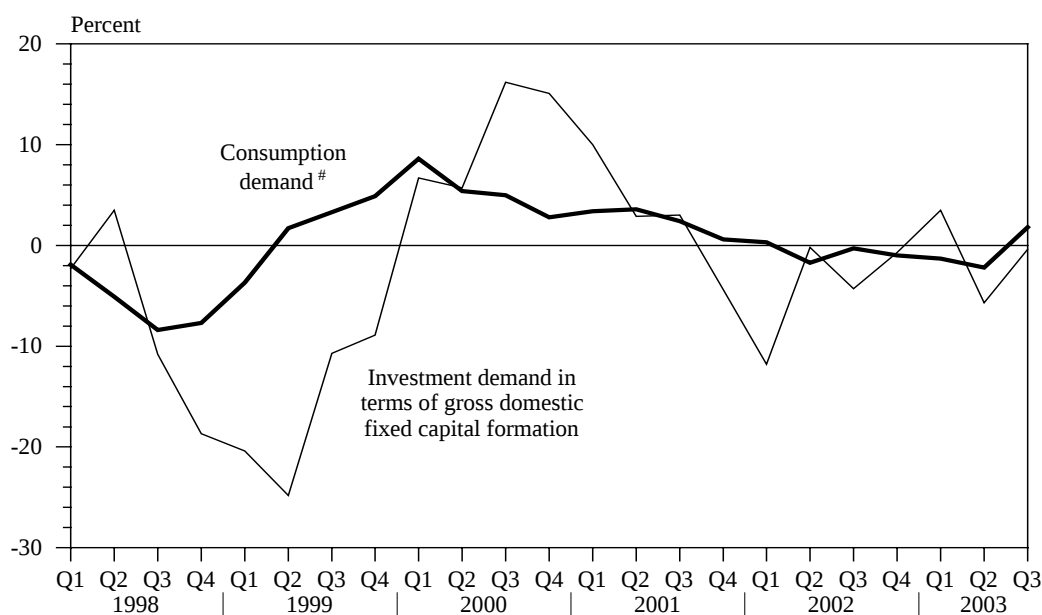
(b) This is a broad estimate of spending by non-residents in the domestic market, as a deduction item within private consumption expenditure amongst the expenditure components of GDP. The series has been revised, incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003. For details, see Box 1.1.

() Figures in brackets represent the seasonally adjusted quarter-to-quarter % changes in real terms.

(*) Change of less than 0.5%.

Diagram 1.4

**Domestic demand
(year-on-year rate of change in real terms)**



Note : (#) Comprising private consumption expenditure and government consumption expenditure.

/Box 1.2

Box 1.2

Retail sales vis-à-vis private consumption expenditure

Retail sales statistics are primarily intended to measure the sales receipts of goods sold by local retail establishments, for gauging the short-term business performance of the local retail sector. They cover both spending on goods by local households and by tourists in Hong Kong.

Private consumption expenditure (PCE) is a major expenditure component of the Gross Domestic Product (GDP). It is compiled from a wide range of data sources, including the retail sales data. But it has a much broader coverage than retail sales, in that PCE covers consumer spending on goods (purchased from all channels including the conventional retail outlets) as well as spending on services by Hong Kong residents, whether domestically or abroad. As such, the retail sales figures are not as comprehensive and as direct as PCE for gauging the trend in local consumer spending.

More specifically, PCE is distinguished from retail sales statistics in that:

- (1) retail sales statistics refer to consumer spending on goods purchased from local retail establishments, but do not cover those consumer spending on electricity, gas and water and on various services such as housing, transportation, education, medical and health care, recreation, entertainment and personal services. PCE covers households' consumption expenditure on all goods and services;
- (2) visitors' spending in Hong Kong is included in the retail sales figures but not in PCE; and
- (3) Hong Kong residents' consumption expenditure abroad is covered in PCE but such spending being outside Hong Kong is outside the coverage of retail sales statistics.

Due to the differences in coverage, the retail sales and PCE series may not necessarily be very close in terms of trends and fluctuations. As an economy becomes more affluent, consumers tend to spend relatively more on services than on goods. For example, the average proportion spent on food (in particular food for meals prepared at home) is smaller than what it used to be some decades ago. New items like charges for mobile phone services and Internet services now also appear in the spending list of an average household. For households in general, a significant proportion of consumption services are "necessities" such as housing, transportation, and medical and education services, which tend to have a steady growth in demand over time. On the other hand, households tend to spend less on expensive items like motor vehicles and jewellery during economic downturns. Thus, the cyclical pattern of consumer spending on some of the services tends to be less pronounced as compared to that of spending on goods.

1.21 *Government consumption expenditure (GCE)* reckoned on a national accounts basis⁽⁶⁾ went up by 0.5% in real terms in the third quarter of 2003 over a year earlier, broadly similar to the 0.4% increase in the second quarter. On a seasonally adjusted quarter-to-quarter comparison, GCE rose by 1.8% in real terms in the third quarter of 2003, following a decline of 0.3% in the second quarter.

/1.22

1.22 Overall investment spending, as represented by *gross domestic fixed capital formation (GDFCF)*, had a marginal decline of only 0.4% in real terms in the third quarter of 2003 over a year earlier, much smaller than the 5.7% decrease in the second quarter. This improvement was attributable to a visible rebound in *expenditure on machinery, equipment and computer software*, which went up by 4.9% in real terms in the third quarter of 2003 over a year earlier, reversing the 2.0% decline in the second quarter. In part, it was helped by the intake of some aircraft ordered earlier. On the other hand, *expenditure on building and construction* remained slack, falling by 6.4% in real terms in the third quarter of 2003 over a year earlier, having declined by 8.4% in the second quarter. Several major civil engineering projects had wound down or were close to completion, including the first berth of Container Terminal 9 in the private sector, as well as KCR's West Rail, Ma On Shan Extension and Tsim Sha Tsui Extension in the public sector. Also, building activity in the private sector continued to shrink, amidst a dearth of new building projects.

1.23 Having been accumulated for five consecutive quarters, *inventories* fell back in the third quarter of 2003, as import intake for local use dwindled for most of the quarter while overall demand in the local market staged an upturn.

The Government account

1.24 In the first half of the financial year 2003/04 (April to September 2003), *government revenue* amounted to \$45.9 billion, down by 5.6% in money terms from the same period in the financial year 2002/03. Within this total, revenue from salaries tax fell more significantly, due to implementation of a salaries tax rebate under the package of relief measures announced in April. Concurrently, revenue from other major sources such as profits tax, stamp duties and land sales also went down. As to revenue from general rates, it bounced back sharply in the quarter April-June over a year earlier, upon dissipation of the effect of the rates concession granted in 2002. It then fell off again in the quarter July-September over a year earlier, due to another rates concession under the package of relief measures granted in 2003.

1.25 On the other hand, *government spending* in the first half of the financial year 2003/04, at \$120.2 billion, was up by 0.7% in money terms over the same period in the financial year 2002/03. Within this total, capital expenditure rose by 14.9% to \$22.4 billion, including extra expenditure incurred to re-vitalise the

/economy

economy and to provide additional employment and training opportunities after SARS. It more than offset a further decline in recurrent spending, by 2.1% to \$97.8 billion.

1.26 The *fiscal balance* gave a deficit of \$74.3 billion in the first half of the financial year 2003/04, larger than that of \$70.8 billion in the first half the financial year 2002/03. This was largely related to the earlier economic setback owing to SARS, as well as the two packages of relief and support measures announced in April and June.

The property market

1.27 Activity in the sales market for *residential property* showed a strong pick-up during the third quarter of 2003. Sentiment improved markedly, along with the better performance of the overall economy and the strong rally in the stock market. This was particularly so after the signing of CEPA in June and implementation of the “individual visit” scheme for Mainland visitors to Hong Kong in July. Expectation for further policy measures to stabilise the housing market also provided some support. Developers resumed sales in the primary market, which had been held off during the spread of SARS, and the sales were generally met with a good response. In view of this favourable turn, many developers had reduced or withdrawn the price discounts and other concessions they offered earlier. Moreover, there was a notable revival in activity in the secondary market. Flat prices appeared to have bottomed out in the third quarter, with a slight increase recorded in September. In the luxury end of the market, the rebound was more clearly visible. Purportedly, the Government’s new policy measure to attract investment immigrants to Hong Kong rendered some lift to this segment. As to the rental market, leasing activity likewise increased in the third quarter. Flat rentals also appeared to have stabilised towards the end of the quarter (paragraph 3.7).

1.28 On a quarter-to-quarter comparison, the fall in flat prices narrowed, on average to 2% in the third quarter of 2003, from that of 5% in the second quarter. The fall in flat rentals likewise narrowed, on average to 2% in the third quarter of 2003, from that of 4% in the second quarter. For the first three quarters of 2003 as a whole, flat prices on average went down by 10%, and flat rentals by 9%. Compared with the respective peak levels in the third quarter of 1997, flat prices and rentals in the third quarter of 2003 remained substantially lower, by an average of 66% and 49% respectively (paragraph 3.8).

/1.29

1.29 On *commercial property*, both the sales and rental markets for *office space* turned more active in the third quarter of 2003. Investor interest was rekindled somewhat, stimulated in part by the signing of CEPA in June. Leasing demand also strengthened slightly. In addition, more tenants were willing to relocate their offices from buildings which were older or in secondary locations to better ones, as rentals of Grade A office space had fallen to a more attractive level to them. Yet the abundant supply of new and existing office space in overall terms continued to exert a drag on prices and rentals. Meanwhile, the sales and rental markets for *shopping space* both showed a mixed performance in the third quarter of 2003. Retail premises in popular locations and in better-managed shopping malls fared better, supported by the recovery in local consumer demand and in inbound tourism from the earlier SARS impact. Yet the sales and rental markets for *industrial property* remained generally sluggish in the third quarter. Nevertheless, projects involving the conversion of industrial sites to hotel use gained some momentum, amidst the rebound in inbound tourism (paragraphs 3.9 to 3.11).

1.30 Comparing the first nine months of 2003 with a year earlier, *planned developments* of all types of property in the private sector turned up to an increase of 26%, following a marginal decrease of 1% in 2002. Within this total, planned developments of private residential property rose significantly, by 74% in terms of units or by 23% in terms of total usable floor area in the first three quarters of 2003 over a year earlier. Planned developments of property in the “others” category surged even more, by 372%. Yet planned developments of commercial property and industrial property were substantially down, by 55% and 100% respectively (paragraph 3.16).

The labour market

1.31 Labour market conditions, having deteriorated markedly during the second quarter and the beginning of the third quarter under the severe impact of SARS, showed a visible improvement towards the end of the third quarter, as SARS had come under control and as overall economic activity staged a progressive upturn. The *seasonally adjusted unemployment rate* fell back to 8.3% in the third quarter of 2003, following a leap from 7.5% in the first quarter to 8.6% in the second quarter and further to a historical high of 8.7% in May - July. The number of unemployed persons (not seasonally adjusted) likewise dropped, to 297 300 in the third quarter of 2003, after elevating from

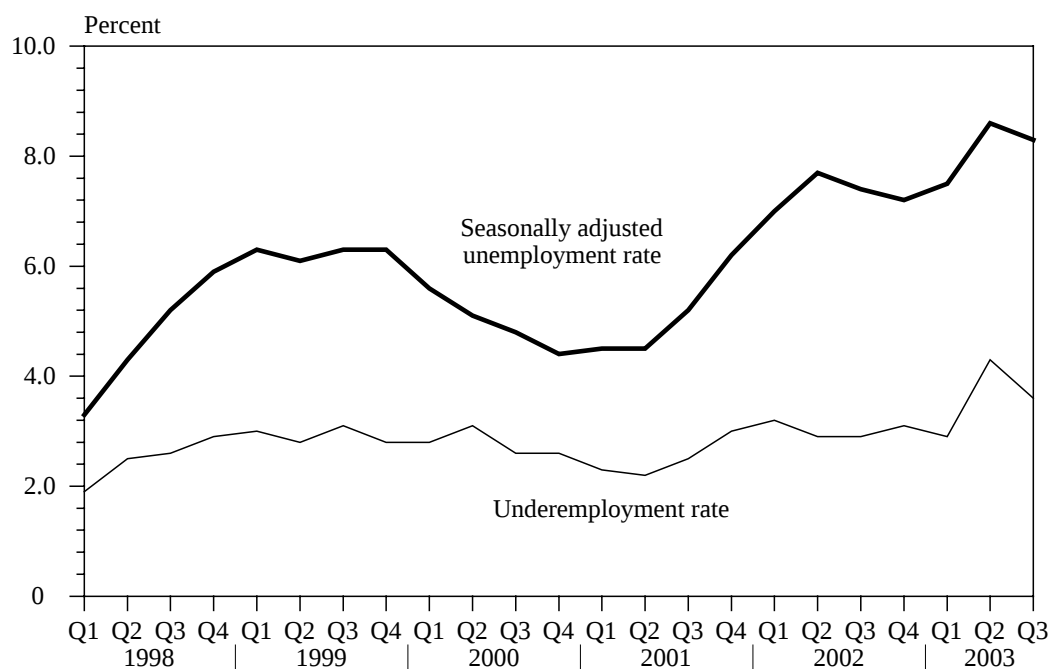
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259 800 in the first quarter to 300 000 in the second quarter and further to a peak of 309 400 in June - August. However, the median duration of unemployment lengthened from 82 days to 90 days between the second and third quarters of 2003, along with an increase in the proportion of persons unemployed for six months or more from 28% to 31%. (In August - October 2003, the seasonally adjusted unemployment rate had a further fall, to 8.0% (provisional).) (paragraph 5.1)

1.32 The *underemployment rate* concurrently declined, to 3.6% in the third quarter of 2003, after leaping from 2.9% in the first quarter to 4.3% in the second quarter. Conceivably, many of the affected employees, having earlier been suspended from work or asked to take no-pay leave, had returned to their jobs more recently. This was notably so for those workers engaged in the tourism and consumption-related sectors. The number of underemployed persons likewise decreased, to 126 600 in the third quarter of 2003, following a lift from 100 700 in the first quarter to 151 000 in the second quarter. (In August - October 2003, the underemployment rate went down further, to 3.5% (provisional).) (paragraph 5.2)

Diagram 1.5

Unemployment and underemployment rates

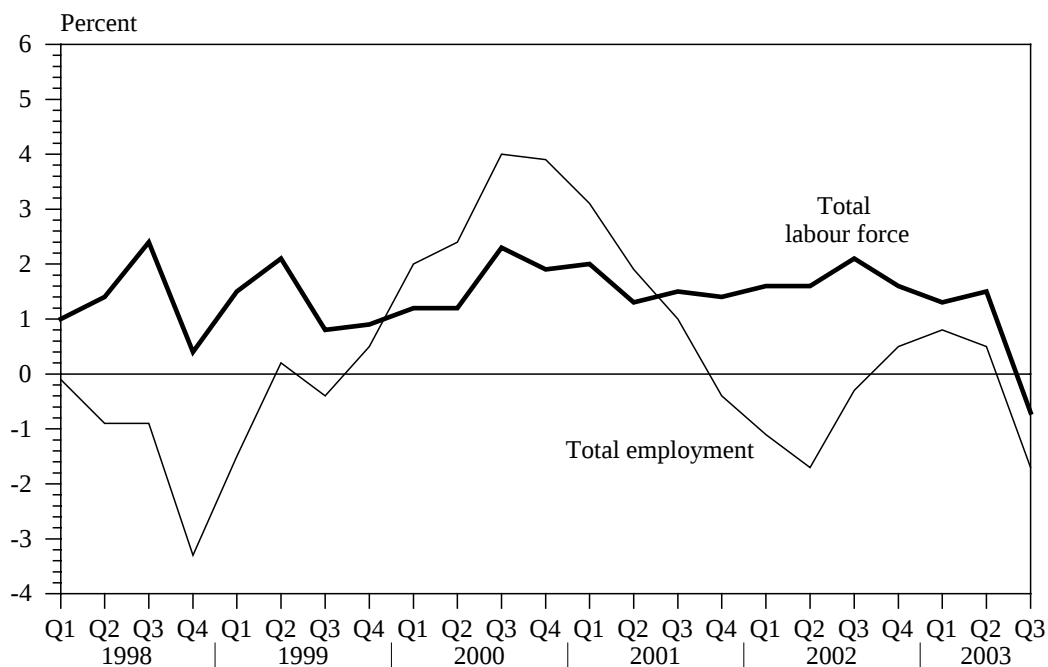


/1.33

1.33 On a quarter-to-quarter comparison, *total employment* as enumerated from households was reduced further, by 0.8% in the third quarter of 2003, following a 0.7% decrease in the second quarter. Weakened labour demand in manufacturing and in foundation and superstructure construction was a major contributory factor. The former could be due to further relocation of production processes outside Hong Kong, and the latter due to completion or winding down of some major construction projects. Yet employment gains were still found in quite a number of economic sectors including restaurants, real estate, the wholesale trade and business services, along with the pick-up in business activity. As to labour supply, *total labour force* showed a distinct moderation, to a 0.8% decrease in the third quarter of 2003, from a 0.5% increase in the second quarter. This reflected the combined influence of a contraction in the population of working age and a decline in the labour force participation rate especially for middle-aged females. On a year-on-year comparison, total employment and total labour force both fell, by 1.7% and 0.7% respectively in the third quarter of 2003, having expanded by 0.5% and 1.5% in the second quarter (paragraph 5.4).

Diagram 1.6

**Total labour force and total employment
(year-on-year rate of change)**



/1.34

1.34 Labour income drifted lower in the second quarter, as the labour market slackened distinctly further under the adverse impact of SARS. Specifically, *labour earnings* decreased by 2.5% in money terms in the second quarter of 2003 from a year earlier, after a 2.0% drop in the first quarter. Netting out the decline in consumer prices as measured by the Composite CPI, labour earnings were down by only 0.1% in real terms in the second quarter of 2003 from a year earlier, having shown nil change in the first quarter. Likewise, *labour wages* were reduced by 2.5% in money terms in June 2003 from a year earlier, following a 1.5% fall in March. Netting out the decline in consumer prices as measured by the CPI(A), labour wages receded also by only 0.1% in real terms in June 2003, following a 0.3% rise in March (paragraph 5.5).

Prices

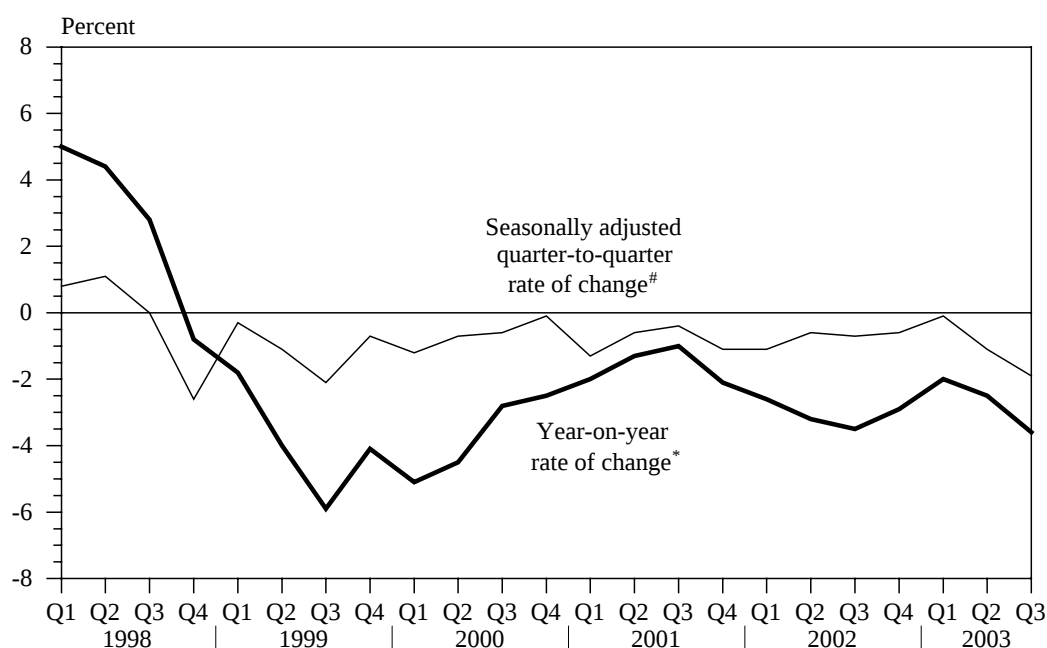
1.35 Overall consumer prices declined further in the third quarter of 2003, thereby extending their downtrend to almost five years. Though with a pick-up in overall economic activity and improving consumer spending during the quarter, local retailers and service providers continued to restrain the prices of their goods and services. Price discounts and other concessions were still widespread, yet apparently with some modest narrowing by the end of the quarter. Meanwhile, the pressure on domestic costs remained scant, as property rentals and labour wages stayed subdued. In addition, there was a dampening effect on the respective costs to consumers brought about by the rates concession and the waiver of water and sewage charges granted by the Government for the periods July - September and August - November respectively. These factors taken together outweighed the pressure due to higher prices of retained imports brought about by a weaker US dollar and firmer world commodity prices (paragraph 6.1).

1.36 On a year-on-year comparison, the *Composite Consumer Price Index* went down by 3.6% in the third quarter of 2003, exceeding the 2.5% fall in the second quarter. The enlarged drop was mainly attributable to the Government's relief measures, specifically the rates concession and the waiver of water and sewage charges, which had the combined effect of lowering the Composite CPI by about one percentage point in the third quarter. For the first nine months of 2003 as a whole, the Composite CPI slid by 2.7% from a year earlier, which was nevertheless less than the 3.0% dip in 2002 (paragraph 6.2).

/Diagram 1.7

Diagram 1.7

Composite Consumer Price Index



Notes : (*) From the fourth quarter of 2000 onwards, the year-on-year changes in the Composite CPI are computed from the new 1999/2000-based series. Before then, the year-on-year changes are computed from the old 1994/95-based series. Splicing has been applied to the indices to maintain continuity.

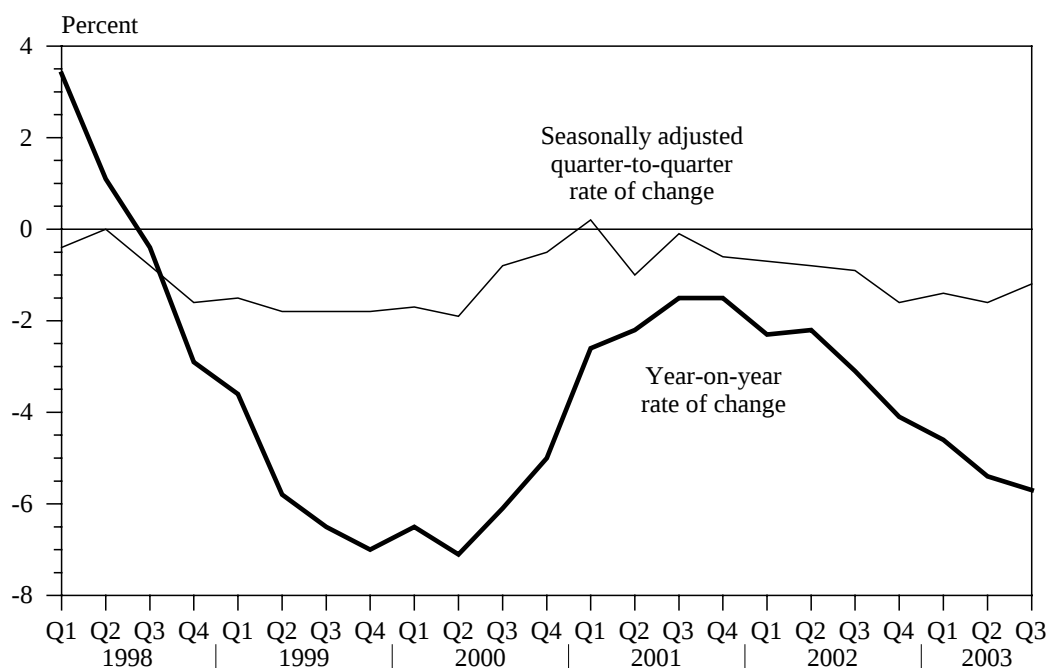
(#) From the first quarter of 2000 onwards, the quarter-to-quarter changes in the seasonally adjusted Composite CPI are computed from the new 1999/2000-based series. Before then, the quarter-to-quarter changes are computed from the old 1994/95-based series. Splicing has been applied to the indices to maintain continuity.

1.37 The *GDP deflator*, as a broad measure of overall price change in the economy, declined by 5.7% in the third quarter of 2003 over a year earlier, even larger than the 5.4% fall in the second quarter. This was mainly due to enlarged declines in the price deflator for private consumption expenditure and for gross domestic fixed capital formation, more than offsetting lesser deterioration in the terms of trade in goods and in services. Within the GDP deflator, the *domestic demand deflator* and the *total final demand deflator* both had enlarged declines, by 4.5% and 3.1% respectively in the third quarter of 2003 over a year earlier as against 4.1% and 2.8% in the second quarter. On a seasonally adjusted quarter-to-quarter comparison, the GDP deflator fell by 1.2% in the third quarter of 2003, which was nevertheless smaller than the 1.6% decrease in the second quarter (paragraph 6.17).

/Diagram 1.8

Diagram 1.8

GDP deflator



The financial sector

1.38 The spot *exchange rate of the Hong Kong dollar* against the US dollar stayed on the strong side of the linked rate (at 7.80) throughout the third quarter of 2003. It appreciated more visibly towards the end of the quarter, reaching 7.749 on 23 September and hovering at around that level towards end-September. The spread of the twelve-month forward rate against the spot rate switched from a premium to a discount of 105 pips (each pip equivalent to HK\$0.0001) also on 23 September. The discount narrowed to 79 pips at end-September, which contrasted with a premium of 120 pips at end-June. The fluctuations in the Hong Kong dollar exchange rate in the latter part of September were affected by more intense rumours for revaluation of the renminbi (paragraph 4.2).

1.39 Under the linked exchange rate system, the movements in the exchange rates of the Hong Kong dollar against other major currencies follow closely those in the US dollar. During the third quarter of 2003, the US dollar weakened against most of the East Asian currencies, amidst concerns about the worsening US trade deficit. In particular, the yen - dollar rate fell by 2.8% from a monthly average of 118.3 in June to that of 115.0 in September. The US dollar also eased

/against

against the Thai baht, the Korean won and the New Taiwan dollar by 2.8%, 2.4% and 1.9% respectively. Yet it strengthened against the major European currencies. The dollar - euro rate appreciated by 3.5% from a monthly average of 1.167 in June to that of 1.130 in September, and the dollar - pound sterling rate by 2.8% from a monthly average of 1.661 to that of 1.614 between these two months. Taking these currency movements together, the trade-weighted *Nominal Effective Exchange Rate Index of the Hong Kong dollar* went up marginally by 0.1%, from a monthly average of 100.56 in June to 100.63 in September. However, after adjusting for changes in the respective consumer price indices, the trade-weighted *Real Effective Exchange Rate Index of the Hong Kong dollar* was down by 2.2%, from 90.0 to 88.0 over the same period (paragraphs 4.3 and 4.4).

1.40 Higher liquidity in the banking sector resulting from increased inflow of funds pushed down the local inter-bank *interest rates* during the third quarter of 2003. At end-September, the three-month HIBOR closed at 0.7%, down from 1.0% at end-June. Over the same period, the negative spread of the three-month HIBOR against the corresponding Euro-dollar deposit rate widened, from 6 basis points to 44 basis points. As the US Fed Funds target rate stayed intact at 1% in the third quarter of 2003, the Base Rate under the Discount Window operated by the Hong Kong Monetary Authority also held steady, at 2.5%. The best lending rate and savings deposit rate offered by the major commercial banks likewise remained unchanged, at 5.00% and 0.03% respectively throughout the quarter. There was a marginal widening in the spread of the best lending rate over the three-month time deposit rate, from an average of 4.91 percentage points in the second quarter of 2003 to 4.92 percentage points in the third quarter (paragraphs 4.5 and 4.6).

1.41 *Hong Kong dollar deposits* rose further by 2.4% during the third quarter of 2003, following a 2.1% increase during the second quarter. Yet *Hong Kong dollar loans* decreased further by 1.8% during the third quarter of 2003, after a 0.8% fall during the second quarter. As Hong Kong dollar loans contracted further while Hong Kong dollar deposits expanded further during the third quarter, the Hong Kong dollar loan-to-deposit ratio moved down appreciably further, to 83.2% at end-September, from 86.7% at end-June (paragraphs 4.8, 4.15 and 4.16).

/1.42

1.42 The local *stock market*, having shown a distinct upturn since late April, rose significantly further during the third quarter of 2003. It was underpinned by growing optimism about the performance and near-term outlook of the Hong Kong economy. Further lifting market sentiment were signing of CEPA, implementation of the “individual visit” scheme for Mainland visitors to Hong Kong, and a rebound in activity in the residential property market. Increased inflow of funds into the region gave an additional boost. The general uptrend in the overseas stock markets also contributed. As a result, the Hang Seng Index surged amidst active market trading, reaching a high at 11 296 on 24 September. While profit-taking in the latter part of the month pared some of the earlier gains, the Hang Seng Index managed to close at 11 230 at the end of September, 17.3% higher than the level at end-June, and 33.5% higher than the trough at 8 409 on 25 April. (The Hang Seng Index rose further, to a new high at 12 251 on 21 October, upon further inflow of funds and probably also in the light of the Government’s announcement of additional measures to stabilise the residential property market. It broadly hovered within 11 700 - 12 400 thereafter, with a leap to another new high at 12 441 on 4 November, before settling back to close at 11 845 on 20 November.) Transactions surged to an even larger extent, with the average daily turnover leaping to \$12.0 billion in the third quarter, from \$8.1 billion in the second quarter (paragraphs 4.30 and 4.31).

/Notes

Notes :

- (1) The “individual visit” scheme was first launched to residents of four cities in Guangdong Province, including Dongguan, Zhongshan, Jiangmen and Foshan, on 28 July 2003. This was then extended to residents of Guangzhou, Shenzhen, Zhuhai and Huizhou on 20 August 2003, and further to residents of Beijing and Shanghai on 1 September 2003. Under this scheme, Mainland residents in these cities can apply for travel documents which allow them to make up to two visits to Hong Kong within a period of three months, and to stay in Hong Kong each time for up to seven days. There is no restriction on the number of times that the residents may apply for renewal of the travel documents.
- (2) The Gross Domestic Product (GDP) is an overall measure of net output produced within an economy in a specified period, such as a calendar year or a quarter, before deducting the consumption of fixed capital. In accordance with the expenditure approach to its estimation, GDP is compiled as total final expenditures on goods and services (including private consumption expenditure, government consumption expenditure, gross domestic fixed capital formation, changes in inventories, and exports of goods and services), less imports of goods and services.
- (3) The seasonally adjusted quarter-to-quarter GDP series, by removing the variations that occur at about the same time and in about the same magnitude each year, provides another perspective for discerning the trend, particularly in regard to turning points. A detailed examination reveals the presence of seasonality in the overall GDP and in some of its main components, including private consumption expenditure, government consumption expenditure, exports of goods, imports of goods, exports of services, and imports of services. However, due to the presence of considerable short-term fluctuations, no clear seasonal pattern is found in gross domestic fixed capital formation. Therefore, the seasonally adjusted series of GDP is compiled separately at the overall level, rather than summing up from its main components.
- (4) The main text of CEPA was signed between the Central People’s Government and the Hong Kong SAR Government on 29 June 2003, and the six Annexes on 29 September 2003. On the merchandise trade front, the Mainland under CEPA will accord zero tariff for exports from Hong Kong in 273 Mainland product codes as from 1 January 2004, and for exports from Hong Kong in the other product codes maintained on China’s tariff system meeting the CEPA rules of origin by 1 January 2006. On the service trade front, CEPA will allow earlier and wider market access in the Mainland to Hong Kong companies in 18 services sectors, including accounting services, advertising services, audiovisual services, banking services, convention services, distribution services, freight forwarding agency services, insurance services, legal services, logistics services, management consulting services, medical and dental services, real estate and construction services, securities services, storage and warehousing services, telecommunications value added services, transport services, and tourism services. As to trade and investment facilitation, there will be co-operation in a number of delineated areas, including customs clearance, quarantine and inspection, quality assurance and food safety, small and medium-sized enterprises, Chinese medicine and medical products, e-commerce, trade and investment promotion, and transparency in laws and regulations.

/(5)

- (5) The Gross National Product (GNP) is obtained by adding net external factor income flow, being the income inflow minus the corresponding income outflow, to GDP. External factor income inflow refers to income earned by residents from abroad, while external factor income outflow refers to income earned by non-residents from within the domestic territory. Hence GNP is an overall measure of income earned by the residents of an economy in a specified period, both domestically and from elsewhere. It distinguishes from GDP in that GDP is an overall measure of income earned by both residents and non-residents, from within the domestic territory in a specified period. Factor income comprises direct investment income, portfolio investment income, other investment income, and compensation of employees.
- (6) Government consumption expenditure reckoned on a national accounts basis covers the recurrent expenditure on goods and services incurred by government departments. It also covers the recurrent expenditure of quasi-government non-profit bodies, such as the Hong Kong Trade Development Council, Hong Kong Productivity Council, Hong Kong Tourism Board, Consumer Council and Hospital Authority. On the other hand, it does not include the expenditure of those government departments and statutory entities engaged in the production of goods and services principally for sale to the public, such as the Housing Department, Post Office and Water Supplies Department, and such as the Mass Transit Railway Corporation Limited, Kowloon-Canton Railway Corporation and Airport Authority Hong Kong. Government subventions to the various organisations providing community and welfare services are also excluded, because such expenditure is in the nature of transfer payments and not direct consumption of economic resources.

CHAPTER 2 : THE EXTERNAL SECTOR

Major external influences

2.1 The global economy showed signs of renewed recovery in the third quarter of 2003, as sentiment improved soon after the end of the war on Iraq, as the US economy turned more upbeat, and as the impact of SARS waned in the East Asian region.

2.2 In the US economy, the better-than-expected GDP outturn in the second and third quarters of 2003 and successive releases of more favourable forward indicators generally pointed to a faster pick-up in activity. Business confidence concurrently improved, aided further by the fiscal stimulus measures and the low interest rate environment. The labour market, though still slack in overall terms, also exhibited relative improvement lately. Yet against these positive revelations, the growing US fiscal deficit, with its ensuing pressure on interest rates and hence possible repercussions on the asset markets, was a key risk on sustainability of the recovery. Also arousing increased concern was the widening US trade deficit and current account deficit.

2.3 The EU economy remained weak in the third quarter of 2003. It was mainly dragged down by the subdued domestic sector, amidst weakening employment conditions. Moreover, its exports, especially those to the US market, were on a general declining trend so far this year, being aggravated by the sustained strength of the euro. There was nevertheless some relative improvement in overall economic sentiment more recently.

2.4 In East Asia, the recovery process in the Japanese economy that began in the second half of 2002 gathered further strength during the first three quarters of 2003. The export sector remained relatively resilient, while investment spending picked up strongly. Sentiment was lifted by a gradual fall-back in unemployment and a surge in the stock market. The Mainland economy, having slowed down distinctly in the second quarter of 2003 amidst the severe impact of SARS, rebounded strongly in the third quarter as consumer demand recovered swiftly. The export sector was relatively unaffected and stayed buoyant, while the influx of foreign direct investment continued to be hefty. The other East Asian economies hit earlier by SARS also improved visibly in the third quarter of 2003 from the dip in the second quarter,

/underpinned

underpinned by a strong rebound in domestic demand. All in all, both the global and regional economic environment was more sanguine in the third quarter of 2003 than in the second quarter.

Table 2.1

**Gross Domestic Product of selected major economies
(year-on-year rate of change in real terms (%))**

		<u>United States</u>	<u>European Union</u>	<u>Mainland of China</u>	<u>Japan</u>	<u>Taiwan</u>	<u>Singapore</u>	<u>Republic of Korea</u>
2002	Annual	2.4	1.0	8.0	0.1	3.6	2.2	6.3
	H1	1.8	0.9	7.8	-1.7	2.3	1.1	6.4
	H2	3.1	1.2	8.2	2.0	4.9	3.4	6.3
	Q1	1.4 (1.2)	0.7 (0.4)	7.6	-3.1 (0.1)	0.9	-1.5 (1.7)	6.2 (2.5)
	Q2	2.2 (0.3)	1.1 (0.5)	8.0	-0.3 (0.7)	3.7	3.8 (2.9)	6.6 (1.3)
	Q3	3.3 (1.0)	1.1 (0.3)	8.1	1.7 (1.2)	5.2	3.8 (-1.7)	5.8 (1.0)
	Q4	2.9 (0.3)	1.3 (0.1)	8.3	2.3 (0.4)	4.5	3.0 (0.1)	6.8 (2.0)
2003	H1	2.3	0.7	8.2	3.0	1.7	-1.2	2.7
	Q1-Q3	2.6	0.7	8.5	2.8	2.6	-0.2	2.6
	Q1	2.0 (0.4)	0.9 (*)	9.9	2.9 (0.5)	3.5	1.6 (0.3)	3.7 (-0.4)
	Q2	2.5 (0.8)	0.5 (*)	6.7	3.2 (0.9)	-0.1	-3.8 (-2.5)	1.9 (-0.7)
	Q3	3.3 (1.7)	0.6 (0.4)	9.1	2.5 (0.6)	4.2	1.7 (4.1)	2.3 (1.1)

Notes : Figures in brackets are the seasonally adjusted quarter-to-quarter rates of change. For the mainland of China and Taiwan, seasonally adjusted series are not available.

(*) Change of less than 0.05%.

/Table 2.2

Table 2.2

**Total exports of goods of selected major economies
(year-on-year rate of change in local currency terms (%))**

		<u>United States</u>	<u>European Union</u>	<u>Mainland of China*</u>	<u>Japan</u>	<u>Taiwan</u>	<u>Singapore[#]</u>	<u>Republic of Korea*</u>
2002	Annual	-5.1	1.2	22.4	6.4	8.9	1.9	8.0
	H1	-11.0	0.5	14.1	1.3	4.6	-7.9	-3.3
	H2	1.5	2.0	29.6	11.8	13.3	12.8	20.3
	Q1	-15.1	-2.1	10.0	-3.0	-1.0	-15.0	-11.1
	Q2	-6.7	2.9	17.8	5.7	10.1	-0.4	4.9
	Q3	1.0	3.3	28.7	7.4	16.0	16.1	15.9
	Q4	1.9	0.7	30.5	16.2	10.9	9.7	24.6
2003	H1	3.0	-3.3	34.0	3.9	7.0	15.1	17.4
	Q1-Q3	2.8	-2.7	32.3	5.0	8.5	14.4	17.0
	Q1	4.5	-1.2	33.6	5.1	10.3	20.6	20.8
	Q2	1.6	-5.3	34.3	2.8	4.0	10.1	14.5
	Q3	2.3	-1.4	29.7	7.1	11.3	13.2	16.3

Notes : (#) Non-oil domestic exports.

(*) Data on exports in the mainland of China and the Republic of Korea are in US dollar terms.

Table 2.3

**Imports of goods of selected major economies
(year-on-year rate of change in local currency terms (%))**

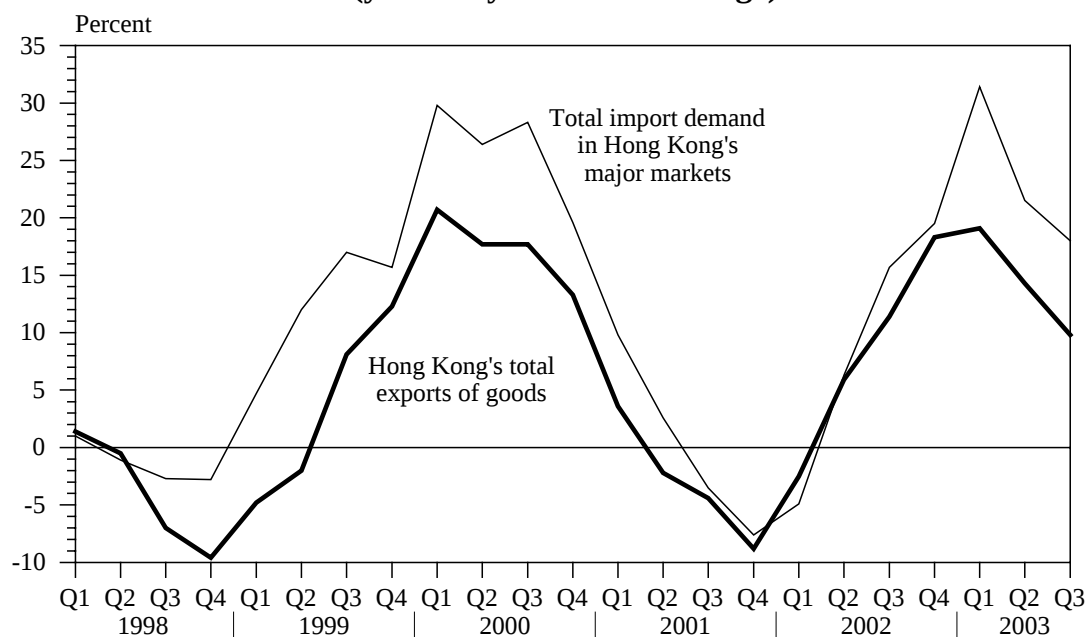
		<u>United States</u>	<u>European Union</u>	<u>Mainland of China*</u>	<u>Japan</u>	<u>Taiwan</u>	<u>Singapore</u>	<u>Republic of Korea*</u>
2002	Annual	1.6	-4.0	21.2	-0.4	7.6	0.4	7.8
	H1	-6.2	-6.8	10.4	-6.3	-1.0	-4.8	-2.2
	H2	10.0	-0.9	31.1	5.8	16.7	5.8	18.5
	Q1	-12.7	-9.1	5.1	-8.2	-8.9	-12.2	-11.4
	Q2	0.5	-4.5	15.0	-4.4	6.8	3.0	7.8
	Q3	7.7	-2.3	29.2	2.1	20.0	5.3	13.8
	Q4	12.3	0.4	33.0	9.4	13.5	6.3	23.1
2003	H1	10.3	-0.3	44.5	7.2	11.5	4.5	21.0
	Q1-Q3	8.6	-0.7	40.5	7.0	9.7	4.5	17.3
	Q1	14.4	3.4	52.3	8.2	18.7	9.5	30.9
	Q2	6.7	-3.9	38.3	6.3	5.4	-0.1	12.1
	Q3	5.4	-1.5	34.3	6.5	6.4	4.6	10.4

Note : (*) Data on imports in the mainland of China and the Republic of Korea are in US dollar terms.

/Diagram 2.1

Diagram 2.1

**Hong Kong's total exports of goods
and total import demand in Hong Kong's major markets
(year-on-year rate of change)**



Note : Total exports of goods as depicted refer to the year-on-year rate of change in real terms, while total import demand in Hong Kong's major markets as depicted refers to the year-on-year rate of change in US dollar terms in the aggregate import demand in East Asia, the United States and the European Union taken together.

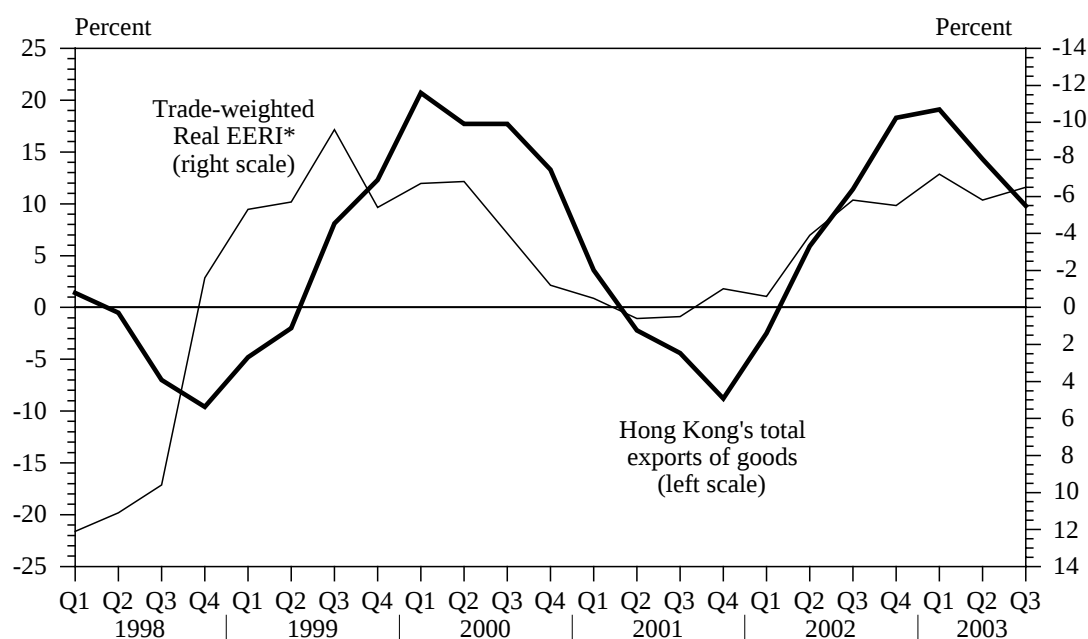
2.5 On exchange rate movements, the US dollar regained some lost ground against the European currencies during the third quarter of 2003, upon a better outlook in the US economy. The trend of rebound in the US dollar reversed as G7's urge for more flexible exchange rates triggered a change in view in the market, causing the US dollar to hit a three-month low against the euro at end-September. Meanwhile, the US dollar was on a general weakening track against the Japanese yen during the third quarter, more so towards the end of the quarter as prospects in the Japanese economy turned more positive. Comparing the average level in the third quarter of 2003 with that in the second quarter, the US dollar still went up by 0.9% and 0.5% respectively against the euro and the pound sterling, yet was 0.9% lower against the Japanese yen. Concurrently, the US dollar also weakened against most of the other East Asian currencies, particularly the Korean won and the Thai baht.

/2.6

2.6 With the movement of the Hong Kong dollar tracking closely that of the US dollar under the linked exchange rate system, and also with a larger price decline in Hong Kong in the more recent months as compared to the earlier months, the trade-weighted Real Effective Exchange Rate Index of the Hong Kong dollar fell further by an average of 3.4% in the third quarter of 2003 over the preceding quarter. This continued to render support to Hong Kong's export performance in recent months by enhancing further Hong Kong's external price competitiveness.

Diagram 2.2

**Hong Kong's total exports of goods and exchange rate movements
(year-on-year rate of change in real terms)**



Note : (*) The Real Effective Exchange Rate Index of the Hong Kong dollar (Real EERI), as compiled by the Hong Kong Monetary Authority, is a weighted average of the exchange rates of the Hong Kong dollar against the currencies of 14 major trading partners after adjusting for relative movements in the respective seasonally adjusted consumer price indices, with the weights adopted being the shares of these 14 trading partners in the overall value of Hong Kong's merchandise trade.

Positive changes in the Real EERI denote real appreciation of the Hong Kong dollar, and negative changes denote real depreciation. For ease of comparison with the rate of change in Hong Kong's total exports of goods, the scale for the Real EERI is presented here upside down, so that positive changes appear at the lower part and negative changes at the upper part of the diagram.

/Table 2.4

Table 2.4

**Exchange rates of the major currencies
and of selected East Asian currencies against the US dollar**

% change in terms of average in the quarter over <u>the preceding quarter</u>		Japanese <u>yen</u>	<u>Euro</u>	Pound <u>sterling</u>	New Taiwan <u>dollar</u>	Singapore <u>dollar</u>	Korean <u>won</u>
2002	Q1	-6.6	-2.0	-1.1	-1.3	-0.4	-2.1
	Q2	4.3	4.7	2.5	1.7	1.6	4.0
	Q3	6.4	7.1	6.0	1.4	2.6	6.0
	Q4	-2.6	1.7	1.5	-2.5	-0.5	-1.9
2003	Q1	2.9	7.2	2.0	0.4	1.3	1.5
	Q2	0.4	5.9	1.0	-0.1	-0.2	-0.6
	Q3	0.9	-0.9	-0.5	1.4	-0.1	2.9

Overall visible and invisible trade situation

2.7 On visible trade, with generally improved global and regional economic environment and with the earlier weakening in the US dollar still giving some positive boost, exports of goods continued to show notable growth in the third quarter of 2003. But the growth pace was not as marked as in the first half of the year, due in part to a higher base of comparison in the third quarter of 2002. *Total exports of goods* (comprising re-exports and domestic exports) had a growth of 7.1% in value terms over a year earlier, to \$465.7 billion in the third quarter of 2003. After netting out the decrease in prices, the growth was 9.8% in real terms⁽¹⁾. On the monthly profile, export growth in real terms was 10.4% in July, 9.8% in August and 9.3% in September. The effect of a higher base of comparison was more appreciable in September, as exports accelerated to a double-digit increase in September last year. Together with a 16.5% surge in the first half of the year, total exports of goods leaped by 13.9% in real terms in the first nine months of 2003 over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, total exports of goods were virtually unchanged in real terms in the third quarter of 2003, after rising for six consecutive quarters and up by 3.2% in the first quarter and 2.4% in the second quarter.

/2.8

2.8 *Re-exports*⁽²⁾ remained the key driver of growth within total exports of goods, leaping by 8.2% in value terms over a year earlier to \$430.6 billion in the third quarter of 2003. After netting out the decrease in prices, there was an 11.3% increase in real terms. There were double-digit increases in real terms for each month of the third quarter, at 12.2%, 11.0% and 10.7% respectively. For the first nine months of 2003 taken together, re-exports soared by 16.3% in real terms over a year earlier, having increased distinctly by 19.4% in the first half of the year. On a seasonally adjusted quarter-to-quarter comparison, re-exports however fell back modestly, by 0.6% in real terms in the third quarter of 2003, having risen by 4.0% and 2.7% respectively in the first and second quarters.

2.9 *Domestic exports* continued to be suppressed by the on-going structural shift towards re-exports and offshore trade⁽³⁾. In the third quarter of 2003, domestic exports fell further, by 5.4% in value terms over a year earlier to \$35.1 billion. After netting out a marginal increase in prices, the decline was also 5.4% in real terms. As to the individual months in the third quarter, the declines in real terms were 7.3%, 2.8% and 6.0% respectively. Along with a 12.3% slump in the first half of the year, domestic exports were down by 9.8% in real terms in the first nine months of 2003 over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, domestic exports nevertheless reverted to increase, up distinctly by 8.2% in real terms in the third quarter of 2003, after declines by 6.3% and 1.8% respectively in the first and second quarters.

/Table 2.5

Table 2.5

**Total exports of goods, re-exports and domestic exports
(year-on-year rate of change (%))**

		<u>Total exports of goods</u>			<u>Re-exports</u>			<u>Domestic exports</u>		
		<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>
2002	Annual	5.4	8.6	-2.7	7.7	10.9	-2.7	-14.7	-11.3	-3.3
	H1	-1.6	1.8	-3.1	0.2	3.5	-2.9	-17.7	-12.5	-4.4
	H2	11.8	14.7	-2.4	14.6	17.7	-2.4	-11.9	-10.2	-2.2
	Q1	-6.2	-2.5	-3.4	-5.0	-1.5	-3.2	-17.5	-11.2	-5.4
	Q2	2.8	5.9	-2.7	5.3	8.3	-2.6	-17.8	-13.7	-3.6
	Q3	8.5	11.4	-2.4	10.6	13.6	-2.3	-10.4	-7.6	-3.1
	Q4	15.5	18.3	-2.3	18.8	22.1	-2.4	-13.6	-12.9	-1.2
2003	H1	14.7	16.5	-1.1	17.2	19.4	-1.3	-11.0	-12.3	0.8
	Q1-Q3	11.8	13.9	-1.4	13.7	16.3	-1.6	-8.9	-9.8	0.6
	Q1	17.6	19.1	-0.9	20.3	22.3	-1.1	-10.4	-12.0	0.8
	Q2	12.2	14.3	-1.4	14.4	17.0	-1.6	-11.4	-12.6	0.7
	Q3	7.1	9.8	-1.8	8.2	11.3	-2.0	-5.4	-5.4	0.3
	Jul	7.6	10.4	-1.7	9.1	12.2	-1.9	-7.1	-7.3	0.5
	Aug	7.0	9.8	-2.0	7.9	11.0	-2.3	-2.4	-2.8	0.6
	Sep	6.4	9.3	-1.7	7.6	10.7	-1.8	-6.9	-6.0	-0.3

Table 2.6

**Total exports of goods, re-exports and domestic exports
(seasonally adjusted quarter-to-quarter
rate of change in real terms (%))**

		<u>Total exports of goods</u>	<u>Re-exports</u>	<u>Domestic exports</u>
2002	Q1	4.5	5.7	-5.6
	Q2	5.8	6.6	-2.0
	Q3	4.0	4.5	-0.7
	Q4	4.0	4.7	-4.3
2003	Q1	3.2	4.0	-6.3
	Q2	2.4	2.7	-1.8
	Q3	*	-0.6	8.2

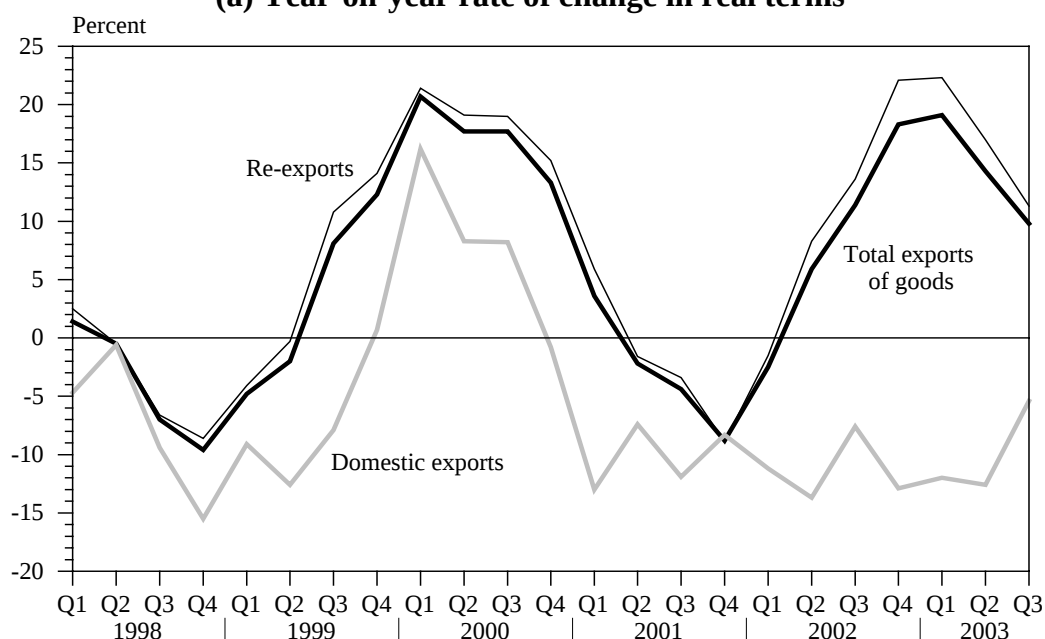
Note: (*) Change of less than 0.05%.

/Diagram 2.3

Diagram 2.3

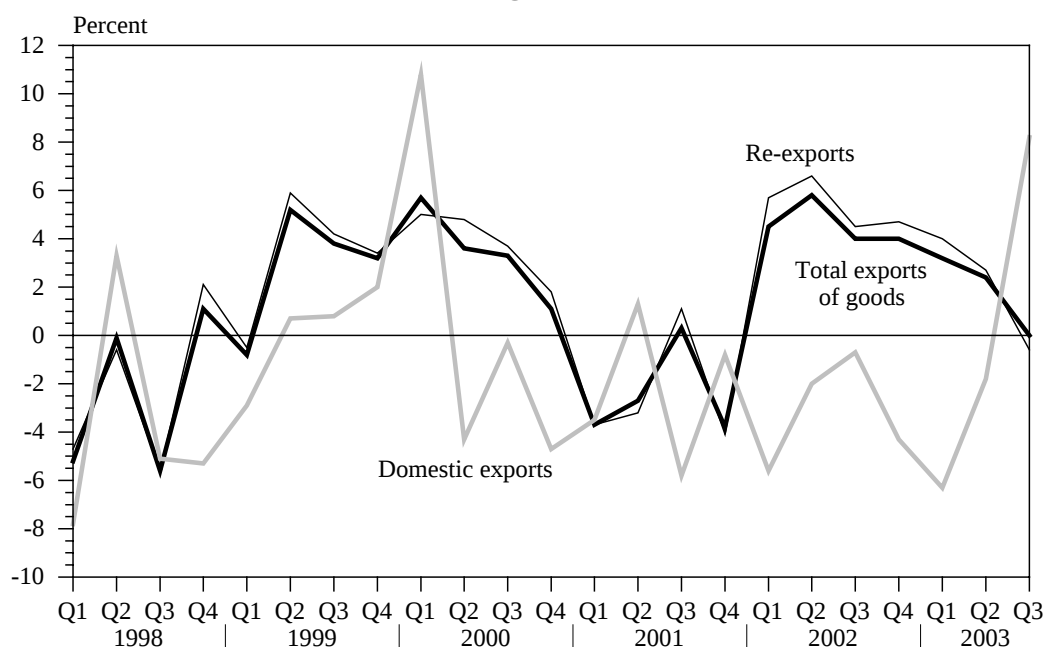
Total exports of goods, re-exports and domestic exports

(a) Year-on-year rate of change in real terms



Note : From the first quarter of 2001 onwards, the rates of change are computed from the new 2000-based trade index series. Before then, the rates of change are computed from the old 1990-based series. Re-scaling using conversion factors as derived from the levels of the old and the new series in their overlapping period of 2000 has been applied to the indices to maintain continuity.

(b) Seasonally adjusted quarter-to-quarter rate of change in real terms



Note : From the second quarter of 2000 onwards, the rates of change are computed from the new 2000-based trade index series. Before then, the rates of change are computed from the old 1990-based series. Re-scaling using conversion factors as derived from the levels of the old and the new series in their overlapping period of 2000 has been applied to the indices to maintain continuity.

/2.10

2.10 *Imports of goods* grew further, by 6.1% in value terms over a year earlier to \$473.1 billion in the third quarter of 2003. After netting out the decline in prices, the increase was 7.9% in real terms. The moderation from the double-digit growth in the preceding four quarters was mainly due to the slow-down in re-export growth from the highly hectic pace in the first half of this year. Also relevant was the continued weakness in imports for local use in most of the third quarter. But as such imports picked up, total imports also rose faster, by 9.2% in real terms in September, as against 7.3% in both July and August. Together with a 14.3% surge in the first half of the year, imports of goods rose by 11.9% in real terms in the first nine months of 2003 over a year earlier. Within total imports, *retained imports* rose back marginally by 0.6% in real terms in the third quarter of 2003 over a year earlier. Such imports were still weak in July and August, down by 2.8% and 0.9% respectively in real terms. A notable rebound to a 5.7% increase occurred in September, as local demand improved. Together with a 4.3% rise in the first half of the year, retained imports went up by 2.9% in real terms in the first nine months of 2003 over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, imports of goods rose back, by 2.2% in real terms in the third quarter of 2003, after a 3.6% increase in the first quarter and a 1.1% decline in the second quarter. Retained imports bounced up more strongly, by 9.3% in real terms in the third quarter of 2003, having risen by 2.9% in the first quarter and plunged by 9.6% in the second quarter.

/Table 2.7

Table 2.7

**Imports of goods and retained imports
(year-on-year rate of change (%))**

		<u>Imports of goods</u>			<u>Retained imports</u> ^(a)		
		<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>
2002	Annual	3.3	7.8	-3.9	-9.0	1.8	-9.7
	H1	-4.2	0.9	-4.8	-15.6	-3.9	-11.7
	H2	10.5	14.3	-3.0	-2.1	7.5	-7.6
	Q1	-9.1	-4.1	-4.9	-19.7	-8.9	-11.6
	Q2	0.4	5.7	-4.6	-11.7	0.8	-11.7
	Q3	6.5	10.8	-3.6	-6.0	5.2	-9.6
	Q4	14.9	18.1	-2.3	2.2	10.0	-5.5
2003	H1	13.4	14.3	-0.2	4.7	4.3	2.4
	Q1-Q3	10.7	11.9	-0.4	3.2	2.9	2.5
	Q1	17.8	18.7	-0.1	11.8	11.5	1.9
	Q2	9.6	10.6	-0.3	-1.5	-1.9	2.8
	Q3	6.1	7.9	-0.9	0.7	0.6	2.7
	Jul	5.6	7.3	-0.8	-3.1	-2.8	2.2
	Aug	6.0	7.3	-0.8	0.9	-0.9	3.6
	Sep	7.3	9.2	-0.9	6.5	5.7	2.1

Note : (a) Based on the results of the Annual Survey of Re-export Trade conducted by the Census and Statistics Department, re-export margins by individual end-use category are estimated and adopted for deriving the value of imports retained for use in Hong Kong.

Table 2.8

**Imports of goods and retained imports
(seasonally adjusted quarter-to-quarter
rate of change in real terms (%))**

		<u>Imports of goods</u>	<u>Retained imports</u> ^(a)
2002	Q1	4.5	2.3
	Q2	5.8	4.2
	Q3	4.8	5.4
	Q4	2.9	-1.0
2003	Q1	3.6	2.9
	Q2	-1.1	-9.6
	Q3	2.2	9.3

Note : (a) See Note (a) to Table 2.7.

/Diagram 2.4

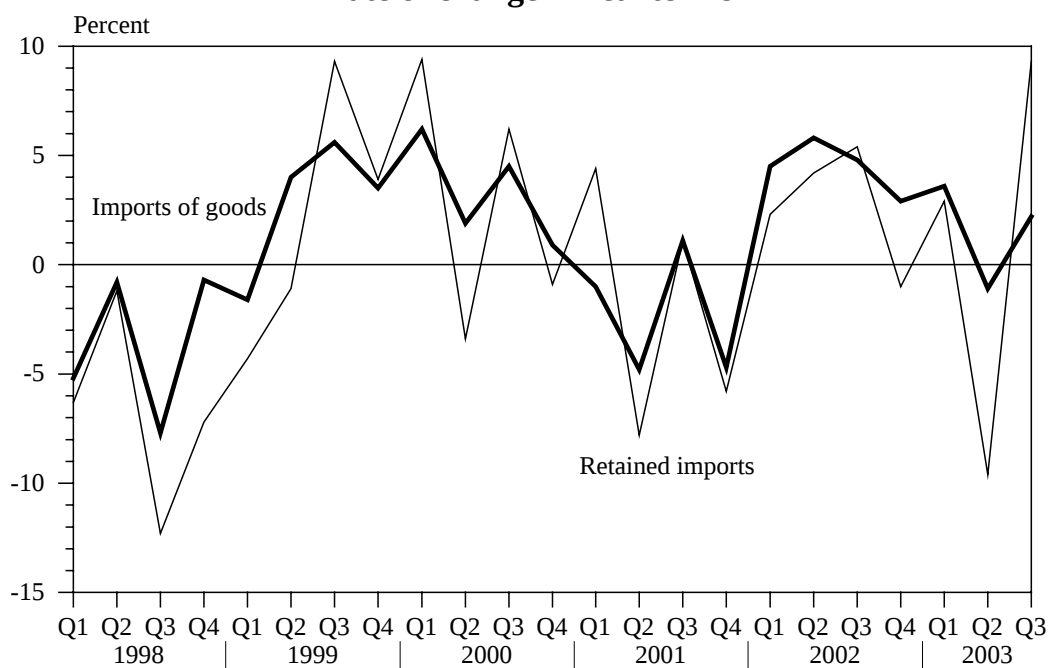
Diagram 2.4

Imports of goods and retained imports
(a) Year-on-year rate of change in real terms



Note : See the footnote to Diagram 2.3 (a).

(b) Seasonally adjusted quarter-to-quarter rate of change in real terms

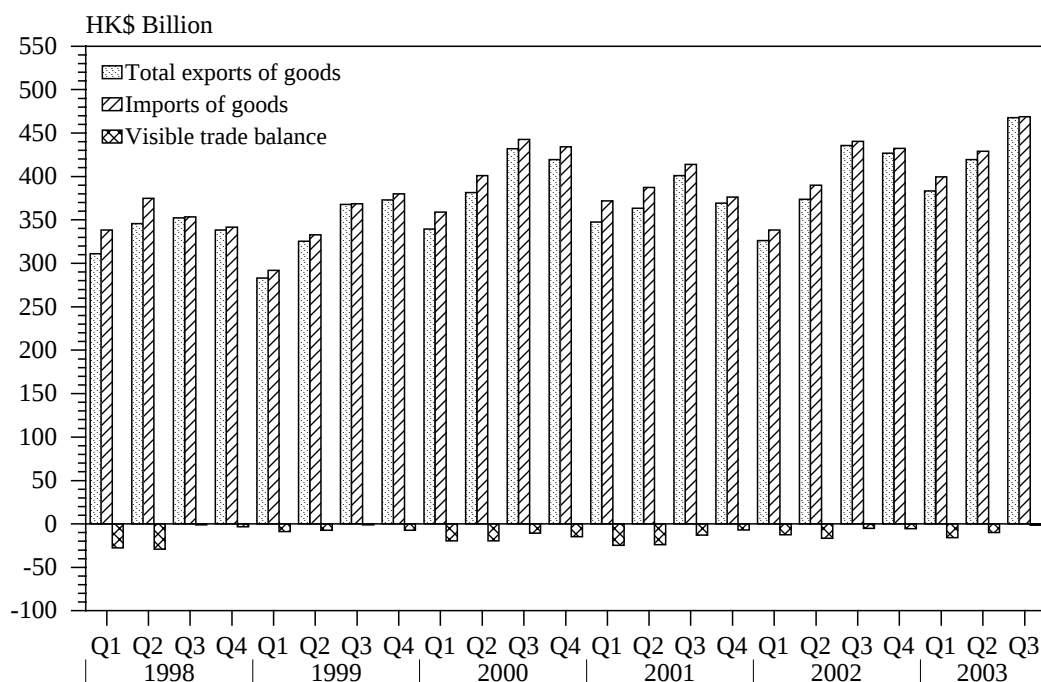


Note : See the footnote to Diagram 2.3 (b).

2.11 With the value of total exports of goods increasing faster than the value of imports of goods, the *visible trade deficit* reckoned on a GDP basis⁽⁴⁾ narrowed further, to \$1.4 billion or 0.3% of the value of imports of goods in the third quarter of 2003, from \$5.0 billion or 1.1% in the same quarter in 2002. For the first nine months of 2003 taken together, the visible trade deficit also narrowed, to \$27.2 billion or 2.1% of the value of imports of goods, from \$33.8 billion or 2.9% in the same period in 2002.

Diagram 2.5

Value of Hong Kong's visible trade and the visible trade balance



/Box 2.1

Box 2.1

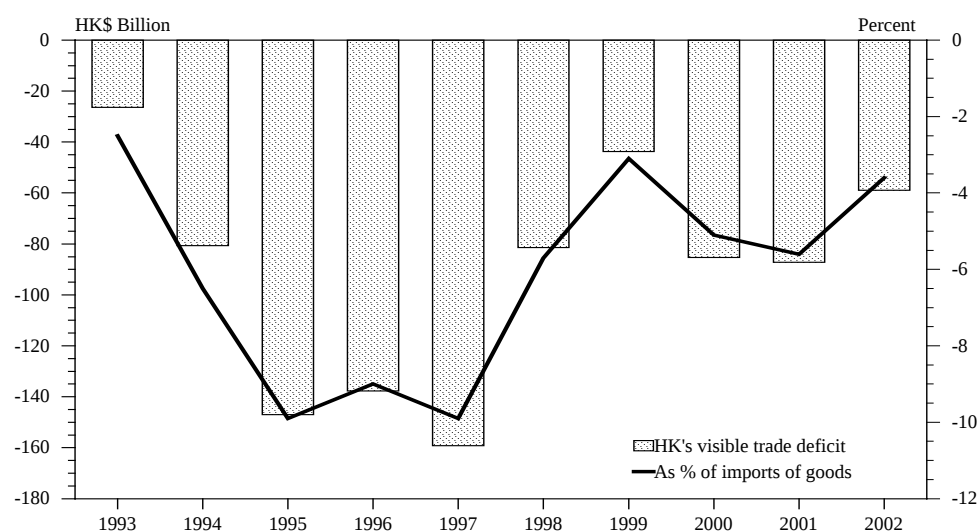
Hong Kong's visible trade balance over the past decade

Hong Kong's visible trade balance was persistently in deficit throughout the past decade (1993-2002).

	Total exports of goods (\$ Bn)	Imports of goods (\$ Bn)	Visible trade balance (\$ Bn)	As % of imports of goods
1993	1,046.3	1,072.6	-26.3	2.5
1994	1,170.0	1,250.7	-80.7	6.5
1995	1,344.1	1,491.1	-147.0	9.9
1996	1,397.9	1,535.6	-137.7	9.0
1997	1,455.9	1,615.1	-159.1	9.9
1998	1,347.6	1,429.1	-81.4	5.7
1999	1,349.0	1,392.7	-43.7	3.1
2000	1,572.7	1,658.0	-85.3	5.1
2001	1,481.0	1,568.2	-87.2	5.6
2002	1,560.5	1,619.4	-58.9	3.6

In terms of the ratio to imports of goods, the deficit was generally rising during the first half of the past decade. It was particularly large in 1995 - 1997, mainly due to heavy intake of materials and equipment during intensive construction of the new airport and the airport railway. With completion of the airport infrastructure in mid-1998, the deficit fell back distinctly in the latter part of that year. The deficit dwindled markedly further in 1999, reflecting the adjustment in import intake for local use so as to restore external balance after the pronounced shock from the Asian financial crisis. Then, as the economic recovery process gathered pace, imports for local use firmed up in the course of 2000, and the deficit rose back to a more normal level in that year. The deficit enlarged slightly further in 2001, owing to a setback in exports brought about by the global economic downturn. In 2002, with exports on an upturn whilst imports for local use still remaining slack amidst the weak domestic sector, the deficit was markedly reduced. This in turn lifted the external balance and contributed to the progressive pick-up in GDP over the course of that year.

Hong Kong's visible trade balance over 1993 - 2002



2.12 On invisible trade, *exports of services*, having plummeted sharply during the second quarter upon the impact of SARS, turned up visibly during the third quarter upon the swift revival in inbound tourism and continued buoyant offshore trade. In the third quarter of 2003, exports of services rose back by 4.6% in value terms over a year earlier to \$94.6 billion. After netting out the decline in prices, the increase was 6.9% in real terms. This represented a sharp turnaround from the 13.9% plunge in the second quarter. Together with a 1.0% decline in the first half of the year, there was a 1.9% increase in real terms for the first three quarters of 2003 as a whole over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, exports of services had a much more pronounced surge, by 31.0% in real terms in the third quarter of 2003, having fallen by 2.6% and 20.0% respectively in the first and second quarters.

2.13 *Imports of services* also recovered from the plunge brought about by SARS. There was a 1.7% rise in value terms over a year earlier to \$53.0 billion in the third quarter of 2003. After netting out the increase in prices, imports of services rose by 0.5% in real terms in the third quarter. The sharp turnaround from the 19.6% slump in the second quarter was underpinned by a swift revival in outbound travel and related transportation services. But with an 11.5% dip in the first half of the year, imports of services still fell markedly by 7.3% in real terms for the first three quarters of 2003 as a whole over a year earlier. On a seasonally adjusted quarter-to-quarter comparison, imports of services had an even stronger rebound, rising by 29.7% in real terms in the third quarter of 2003, following decreases of 6.9% and 17.7% respectively in the first and second quarters.

/Table 2.9

Table 2.9

**Exports and imports of services
(year-on-year rate of change (%))**

		<u>Exports of services[^]</u>			<u>Imports of services</u>		
		<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>	<u>In value terms</u>	<u>In real terms</u>	<u>Change in prices</u>
2002	Annual	9.8	12.2	-2.1	0.5	0.2	0.2
	H1	3.7	7.7	-3.8	-3.5	-2.2	-1.3
	H2	15.5	16.1	-0.5	4.5	2.7	1.7
	Q1	1.0	6.3	-5.0	-3.2	-0.7	-2.4
	Q2	6.3	9.1	-2.7	-3.8	-3.8	*
	Q3	13.4	14.0	-0.5	3.5	2.0	1.4
	Q4	17.5	18.1	-0.5	5.5	3.4	2.0
2003	H1	-2.9	-1.0	-1.9	-9.3	-11.5	2.5
	Q1-Q3	-0.1	1.9	-2.0	-5.3	-7.3	2.0
	Q1	11.5	12.5	-0.9	-0.6	-3.9	3.4
	Q2	-16.5	-13.9	-3.0	-18.3	-19.6	1.6
	Q3	4.6	6.9	-2.1	1.7	0.5	1.2

Notes : (^) Revised series after incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003. For details, see Box 1.1 in Chapter 1.

(*) Change of less than 0.05%.

Table 2.10

**Exports and imports of services
(seasonally adjusted quarter-to-quarter
rate of change in real terms (%))**

		<u>Exports of services[^]</u>	<u>Imports of services</u>
2002	Q1	2.5	0.4
	Q2	4.8	-1.6
	Q3	5.9	3.8
	Q4	4.1	1.1
2003	Q1	-2.6	-6.9
	Q2	-20.0	-17.7
	Q3	31.0	29.7

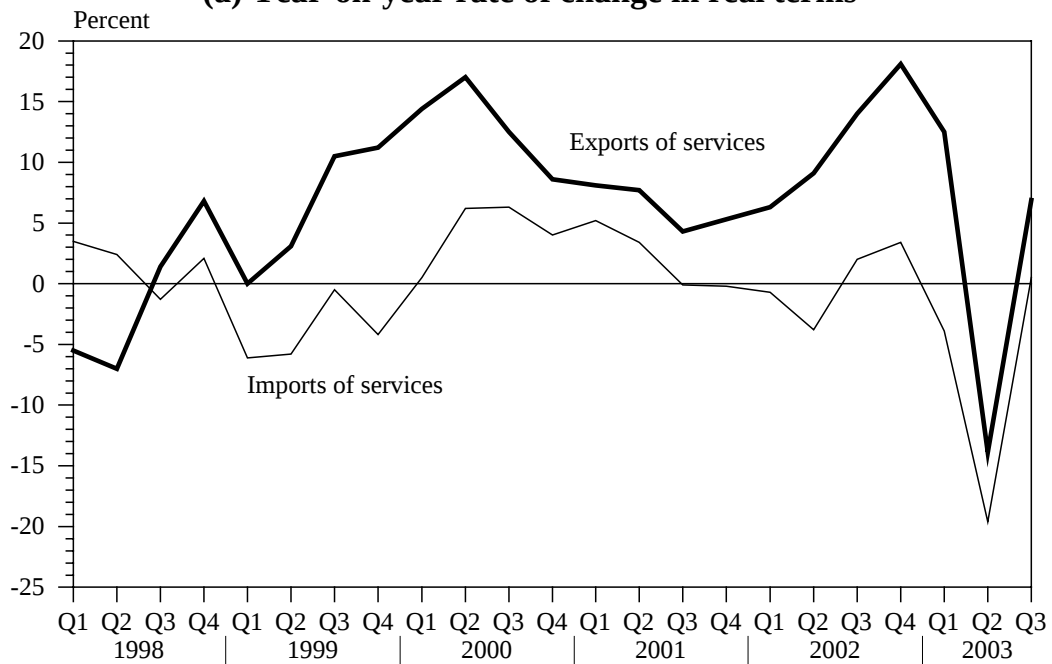
Note : (^) See the first footnote to Table 2.9.

/Diagram 2.6

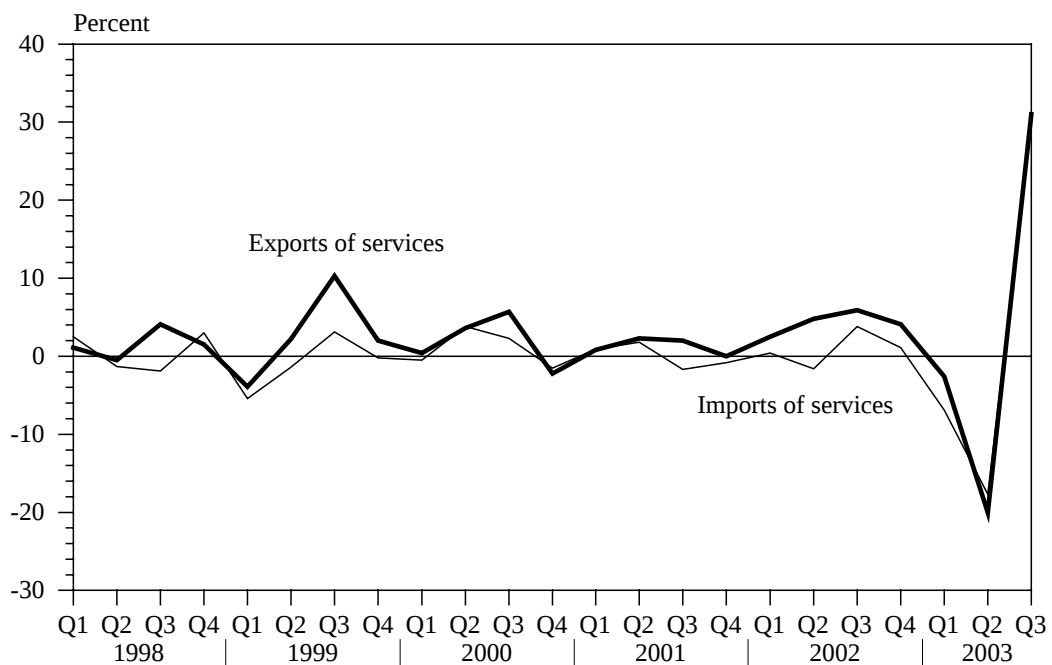
Diagram 2.6

Exports and imports of services

(a) Year-on-year rate of change in real terms



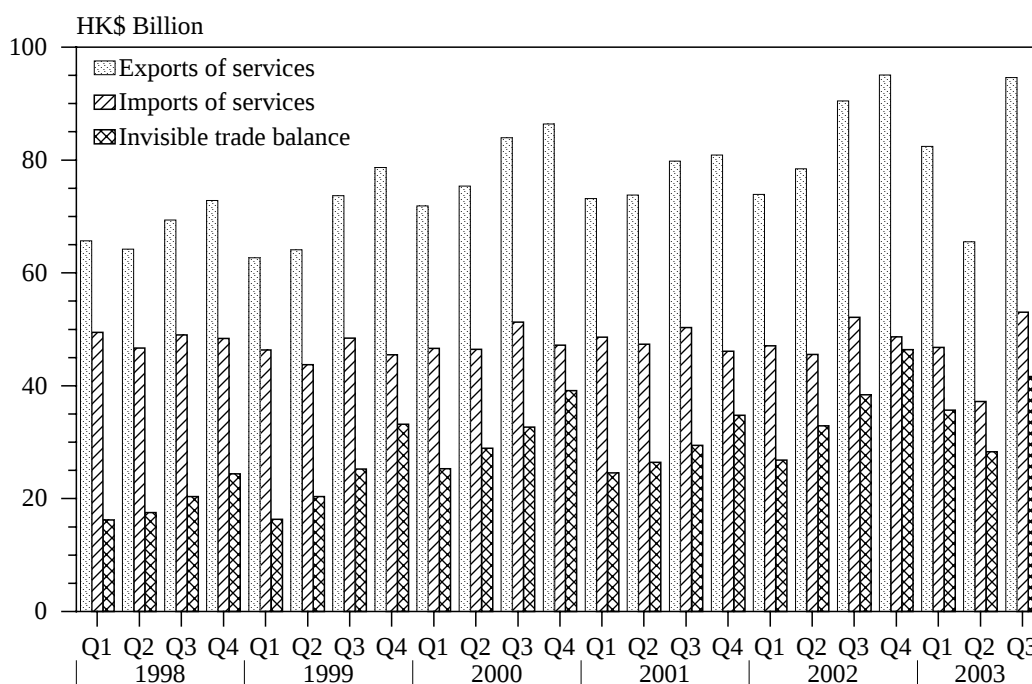
(b) Seasonally adjusted quarter-to-quarter rate of change in real terms



/Diagram 2.7

Diagram 2.7

Value of Hong Kong's invisible trade and the invisible trade balance



2.14 Taking exports and imports of services together, the *invisible trade surplus*⁽⁵⁾ reckoned on a GDP basis rose back to \$41.6 billion or 78.5% of the value of imports of services in the third quarter of 2003, from \$38.4 billion or 73.7% in the same quarter in 2002. For the first three quarters of 2003 as a whole, the invisible trade surplus also enlarged, to \$105.6 billion or 77.1% of the value of imports of services, from \$98.2 billion or 67.8% in the same period in 2002.

2.15 As the visible trade deficit narrowed while the invisible trade surplus expanded, the combined surplus reckoned on a GDP basis surged markedly, to \$40.2 billion or 7.7% of the total value of imports of goods and services in the third quarter of 2003, from \$33.4 billion or 6.8% in the same quarter in 2002. For the first three quarters of 2003 as a whole, the combined surplus went up to \$78.4 billion or 5.5% of the total value of imports of goods and services, as compared to \$64.4 billion or 4.9% in the same period in 2002.

/Table 2.11

Table 2.11

Visible and invisible trade balance
(\$ billion at current market prices)

		<u>Total exports</u>		<u>Imports</u>		<u>Trade balance</u>		
		<u>Goods</u>	<u>Services[^]</u>	<u>Goods</u>	<u>Services</u>	<u>Goods</u>	<u>Services[^]</u>	<u>Combined</u>
2002	Annual	1,562.1	337.9	1,601.5	193.4	-39.4	144.5	105.1
	H1	699.8	152.4	728.6	92.6	-28.8	59.8	30.9
	H2	862.3	185.6	872.9	100.8	-10.6	84.8	74.2
	Q1	326.1	73.9	338.5	47.1	-12.4	26.9	14.4
	Q2	373.7	78.4	390.1	45.5	-16.4	32.9	16.5
	Q3	435.5	90.5	440.5	52.1	-5.0	38.4	33.4
	Q4	426.8	95.1	432.4	48.7	-5.6	46.4	40.8
2003	H1	802.8	147.9	828.6	84.0	-25.8	64.0	38.2
	Q1-Q3	1,270.3	242.6	1,297.5	137.0	-27.2	105.6	78.4
	Q1	383.4	82.4	399.4	46.8	-16.0	35.7	19.7
	Q2	419.3	65.5	429.1	37.2	-9.8	28.3	18.5
	Q3	467.5	94.6	468.9	53.0	-1.4	41.6	40.2

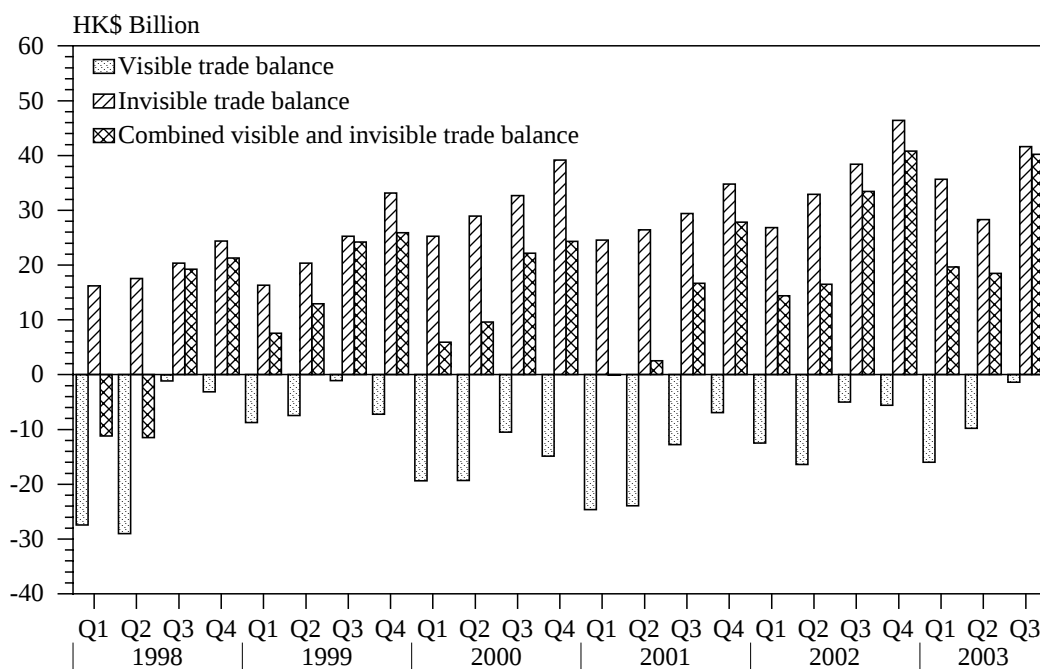
Notes : Figures in this table are reckoned on a GDP basis. Specifically, imports of goods are valued on f.o.b. basis, instead of on c.i.f. basis as is still the on-going practice for the merchandise trade statistics.

Figures may not add up exactly to the total due to rounding.

([^]) See the first footnote to Table 2.9.

Diagram 2.8

Visible and invisible trade balance



Note : See the footnotes to Table 2.11.

/Visible

Visible trade

Total exports of goods

2.16 With its increasingly close trade relations with Hong Kong, East Asia⁽⁶⁾ continued to take up the largest share in Hong Kong's total exports of goods, at 58% by value in the first nine months of 2003. This was followed by North America⁽⁷⁾ (with a share of 20%), and the European Union⁽⁸⁾ (13%).

2.17 Exports to the region remained the key driving force for Hong Kong's export growth. Total exports of goods to *East Asia* as a whole continued to be strong, rising by 17.9% in real terms in the third quarter of 2003 over a year earlier. Together with a 22.2% surge in the first half of the year, exports to the region increased markedly, by 20.6% in real terms in the first nine months of 2003 over a year earlier. Amongst the major markets, exports to the Mainland, the Republic of Korea, Singapore and Taiwan had growth approaching or exceeding 20% in real terms in the third quarter over a year earlier. Exports to Japan, Thailand and Indonesia also maintained double-digit growth. On the other hand, exports to Malaysia and the Philippines slipped into decline.

2.18 Total exports of goods to *North America* slackened further, declining by 6.3% in real terms in the third quarter of 2003 over a year earlier. This reversed the 2.2% rise in such exports in the first half of the year, giving a decline of 1.3% in real terms in the first nine months of 2003 over a year earlier. This went along with the deceleration in US import demand in that quarter. Conceivably also mattered was the further structural shift in re-exports to offshore trade for shipment to the US market.

2.19 Total exports of goods to the *European Union* held up well, with a 10.6% rise in real terms in the third quarter of 2003 over a year earlier, albeit not as marked as the 18.6% surge in the first half of the year. For the first nine months of 2003 taken together, there was a leap of 15.5%. The growth was largely attributable to enhanced price attractiveness of Hong Kong's exports brought about by the strength of the euro.

/Table 2.12

Table 2.12

**Total exports of goods by major region
(year-on-year rate of change in real terms (%))**

		<u>East Asia</u> ^{(a)(d)}	<u>North America</u> ^(b)	<u>European Union</u> ^(c)
2002	Annual	13.4	3.9	-0.4
	H1	7.1	-4.1	-8.1
	H2	19.2	10.8	6.6
	Q1	4.8	-12.4	-12.1
	Q2	9.3	3.5	-3.9
	Q3	14.7	9.5	3.6
	Q4	23.9	12.3	9.7
2003	H1	22.2	2.2	18.6
	Q1-Q3	20.6	-1.3	15.5
	Q1	23.6	9.1	17.8
	Q2	20.9	-3.3	19.4
	Q3	17.9	-6.3	10.6

Notes : (a) For the coverage of East Asia, see Note (6).

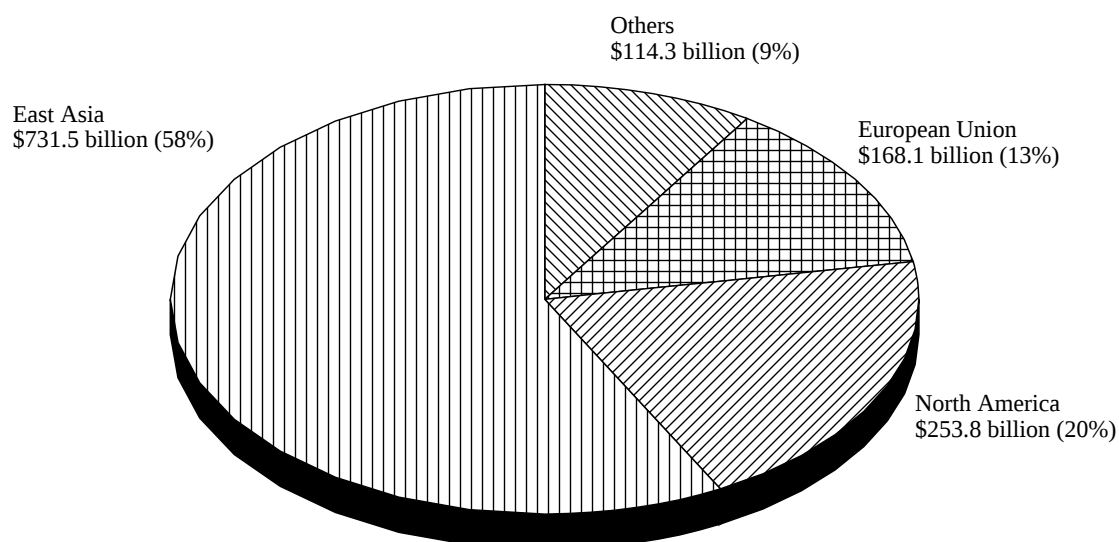
(b) For the coverage of North America, see Note (7).

(c) For the coverage of the European Union, see Note (8).

(d) For those constituent markets where separate quantum indices are not compiled, their levels of total exports of goods in real terms are estimated from an aggregate implicit price deflator covering all those export markets in the Asia-Pacific region for which separate unit value indices are not available.

Diagram 2.9

**Total exports of goods by major region
in the first nine months of 2003**



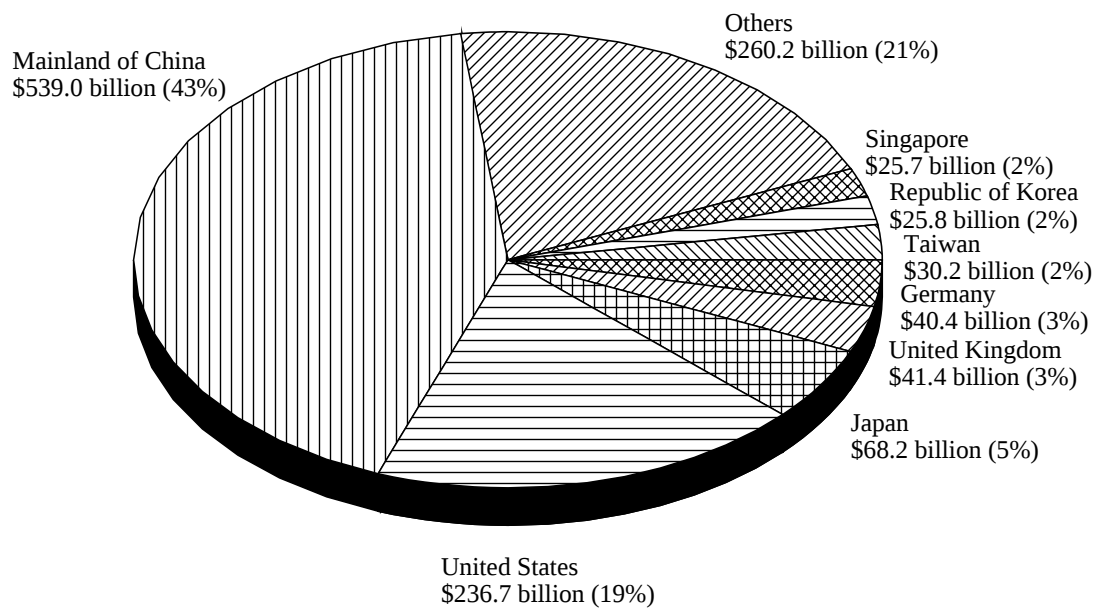
Total exports of goods in the first nine months of 2003 : \$1,267.6 billion

/2.20

2.20 The Mainland continued to be the largest single *market* for Hong Kong's total exports of goods, accounting for 43% of the total value in the first nine months of 2003. This was followed by the United States (with a share of 19%), Japan (5%), the United Kingdom (3%), Germany (3%), Taiwan (2%), the Republic of Korea (2%), and Singapore (2%).

Diagram 2.10

**Total exports of goods by major market
in the first nine months of 2003**



Total exports of goods in the first nine months of 2003 : \$1267.6 billion

/Table 2.13

Table 2.13**Value of total exports of goods by market**

	<u>2002</u>			<u>Jan-Sep 2003</u>		
	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Rate</u> <u>of change</u> (%)	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Year-on-year</u> <u>rate of change</u> (%)
All markets	1,560.5	100	5.4	1,267.6	100	11.8
Mainland of China	613.2	39	12.3	539.0	43	21.0
United States	333.0	21	1.0	236.7	19	-2.6
Japan	83.7	5	-4.5	68.2	5	13.7
United Kingdom	54.2	3	-2.0	41.4	3	5.7
Germany	48.8	3	-5.3	40.4	3	18.0
Taiwan	34.6	2	-2.2	30.2	2	18.8
Republic of Korea	30.4	2	17.2	25.8	2	17.3
Singapore	31.6	2	6.8	25.7	2	11.6
Rest of the world	331.0	21	3.5	260.2	21	7.6

Table 2.14**Total exports of goods by major market
(year-on-year rate of change in real terms (%))**

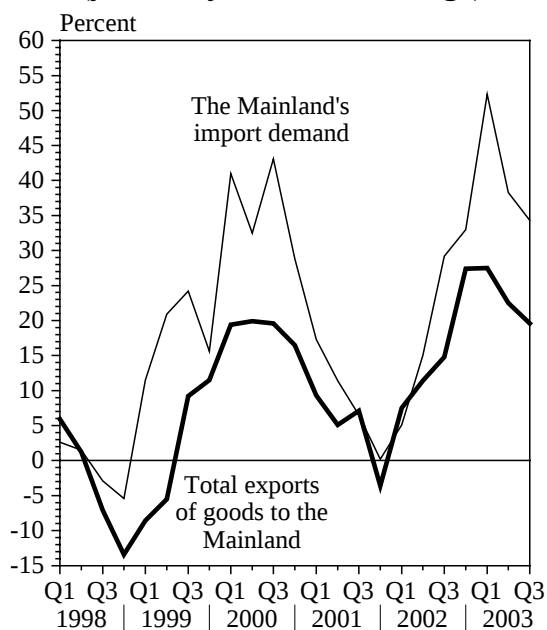
		<u>Mainland</u> <u>of China</u>	<u>United</u> <u>States</u>	<u>Japan</u>	<u>United</u> <u>Kingdom</u>	<u>Germany</u>	<u>Taiwan</u>	<u>Republic</u> <u>of Korea</u>	<u>Singapore</u>
2002	Annual	15.5	3.7	-1.0	0.7	-2.4	2.1	20.8	11.7
	H1	9.5	-4.5	-8.4	-6.0	-11.2	-3.7	16.0	8.5
	H2	20.8	10.8	6.0	6.4	5.3	7.8	25.5	14.7
	Q1	7.5	-13.1	-10.4	-10.7	-16.2	-5.2	16.7	3.4
	Q2	11.4	3.6	-6.1	-1.4	-5.4	-2.2	15.3	14.0
	Q3	14.8	9.9	1.6	5.2	3.9	14.9	22.4	11.4
	Q4	27.4	12.0	10.5	7.7	6.7	1.6	28.3	18.0
2003	H1	24.8	2.0	16.8	8.7	26.1	23.2	19.8	9.9
	Q1-Q3	22.8	-1.4	15.6	8.0	21.4	21.7	20.8	14.4
	Q1	27.5	9.4	15.0	8.5	26.5	26.9	12.4	7.4
	Q2	22.5	-3.7	18.6	8.9	25.8	19.7	27.7	12.3
	Q3	19.6	-6.3	13.5	6.9	14.0	19.1	22.5	22.5
	Jul	21.6	-8.8	18.7	3.3	18.2	24.5	18.9	18.5
	Aug	18.5	-2.1	10.4	7.8	15.9	9.3	25.0	21.3
	Sep	18.7	-7.6	11.3	9.6	8.7	22.9	23.8	27.9

/2.21

2.21 Total exports of goods to the *Mainland* remained on a strong uptrend. After a 24.8% surge in the first half of 2003, there was a further marked growth of 19.6% in real terms in the third quarter of 2003 over a year earlier. Altogether, total exports of goods to this market soared by 22.8% in real terms in the first nine months of 2003 over a year earlier. Intake of materials for export processing remained strong in the third quarter, buoyed by Mainland's surging trade flows. Intake of machinery for production use continued to register robust growth, due in part to activation of the substantial foreign direct investment. Intake of consumer goods also held up well, as domestic demand recovered from the SARS impact.

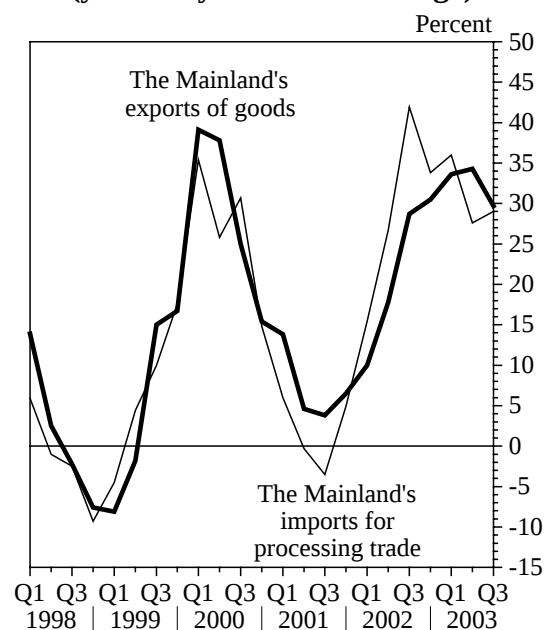
Diagram 2.11

Total exports of goods to the mainland of China and the Mainland's import demand (year-on-year rate of change)



Note : Total exports of goods to this market as depicted refer to the year-on-year rate of change in real terms, while import demand in this market refers to the year-on-year rate of change in US dollar terms.

The Mainland's exports of goods and its imports for processing trade (year-on-year rate of change)

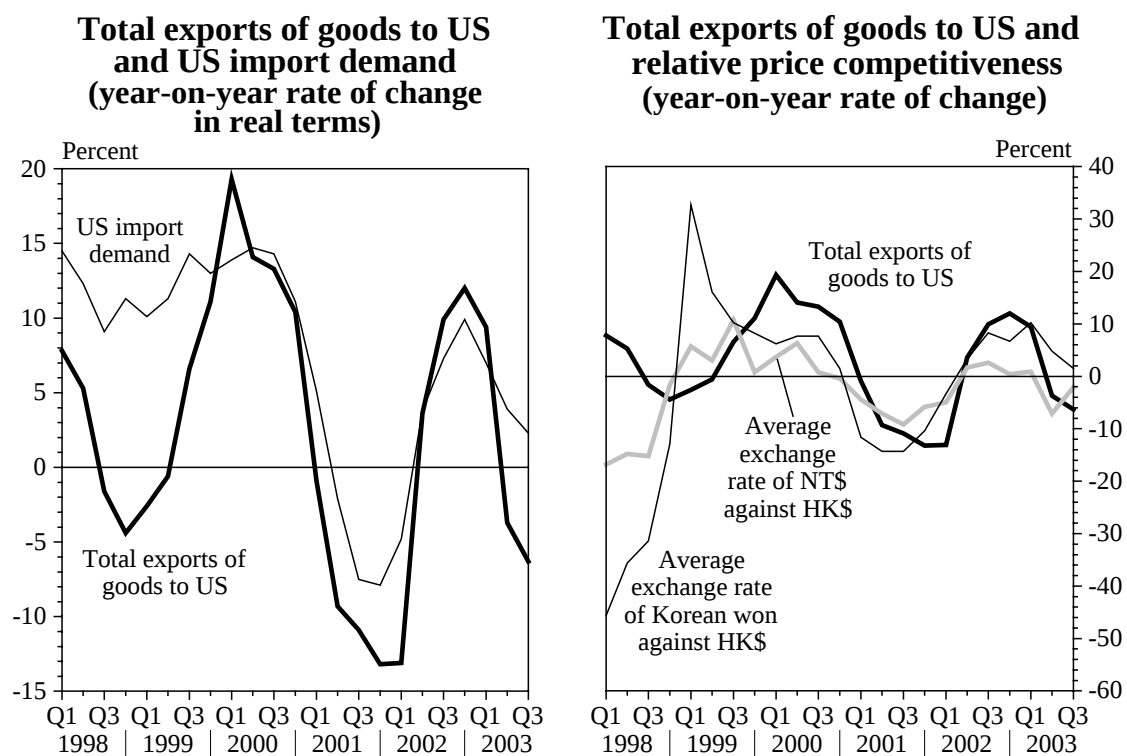


Note : Both refer to the year-on-year rate of change in US dollar terms.

/2.22

2.22 On the other hand, total exports of goods to the *United States* declined all through the third quarter of 2003, cumulating to a further decline of 6.3% in real terms in that quarter over a year earlier. It reversed a modest 2.0% rise in the first half of the year, giving a 1.4% decline in real terms in the first nine months of 2003 over a year earlier. The fall-off in the third quarter was broadly based across all main end-use categories. This was in line with the deceleration in US import demand in that quarter. The further shift away from re-export trade to offshore trade was another relevant factor.

Diagram 2.12



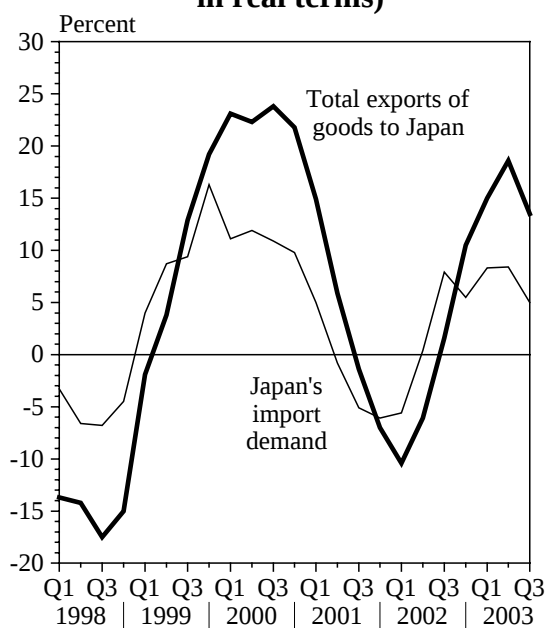
Note : (+) represents appreciation and (-) represents depreciation of the NT\$ and Korean won against HK\$.

/2.23

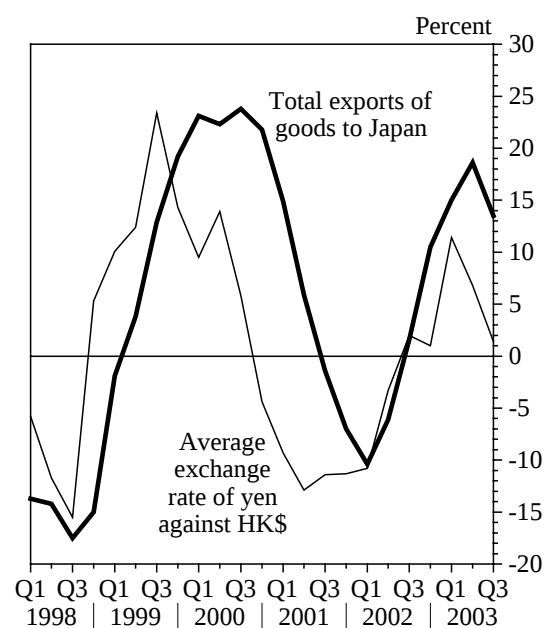
2.23 In contrast, buoyed by a relatively strong yen and generally improving demand, total exports of goods to *Japan* remained robust, surging by 13.5% in real terms in the third quarter of 2003 over a year earlier. This, together with a 16.8% leap in the first half of the year, gave a marked increase of 15.6% in real terms in the first nine months of 2003 over a year earlier. Exports of capital goods and material inputs to Japan were supported much by its resilient export sector. Exports of consumer goods to Japan also held up well.

Diagram 2.13

**Total exports of goods to Japan
and Japan's import demand
(year-on-year rate of change
in real terms)**



**Total exports of goods to Japan
and the exchange rate factor
(year-on-year rate of change)**

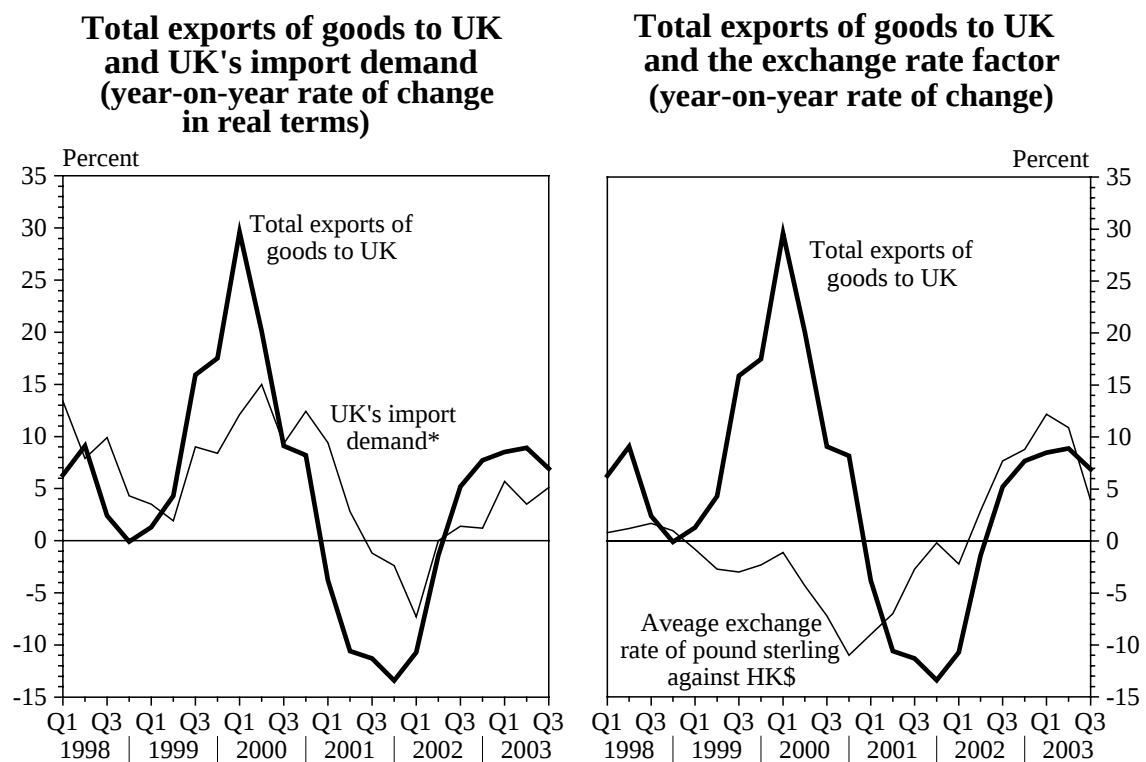


Note : (+) represents appreciation and
(-) represents depreciation of
the yen against HK\$.

/2.24

2.24 Total exports of goods to the *United Kingdom* decelerated somewhat, to a 6.9% growth in real terms in the third quarter of 2003 over a year earlier, from a more distinct growth at 8.7% in the first half of the year. This still gave an 8.0% rise in real terms in the first nine months of 2003 over a year earlier. The performance of exports to this market in the third quarter was in line with the further slow-down in UK's overall import demand, even though the strength of the pound sterling should have rendered some support.

Diagram 2.14



Note : (*) UK's import demand as depicted refers to its imports sourced from outside the European Union.

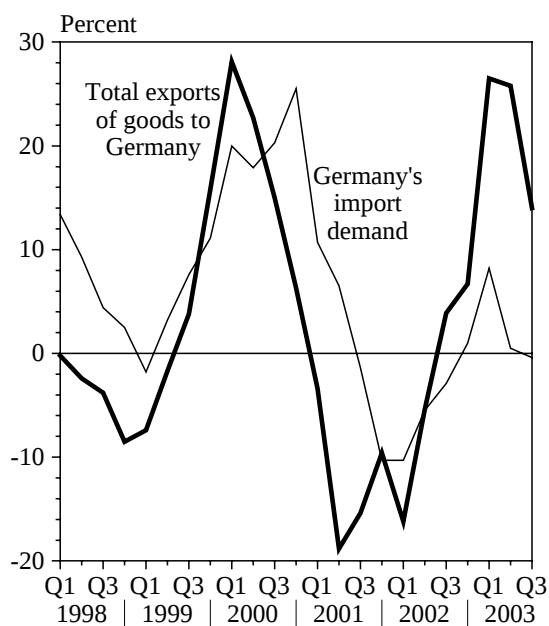
Note : (+) represents appreciation and (-) represents depreciation of the pound sterling against HK\$.

/2.25

2.25 Total exports of goods to *Germany* continued to display strong growth, at 14.0% in real terms in the third quarter of 2003 over a year earlier. Taken together with a 26.1% leap in the first half of the year, total exports of goods to Germany surged by 21.4% in real terms in the first nine months of 2003 over a year earlier. Despite the still modest import demand in Germany, the strength of the euro should have rendered a boost to Hong Kong's exports to this market.

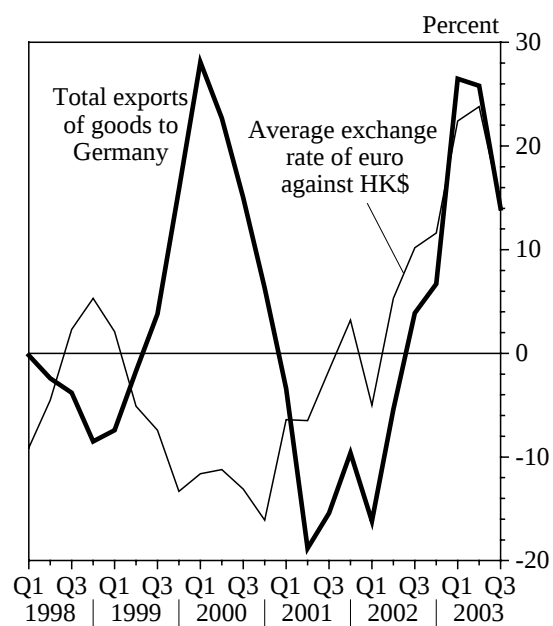
Diagram 2.15

Total exports of goods to Germany and Germany's import demand (year-on-year rate of change)



Note : Total exports of goods to this market as depicted refer to the year-on-year rate of change in real terms, while import demand in this market refers to the year-on-year rate of change in value terms, i.e. in terms of its local currency.

Total exports of goods to Germany and the exchange rate factor (year-on-year rate of change)



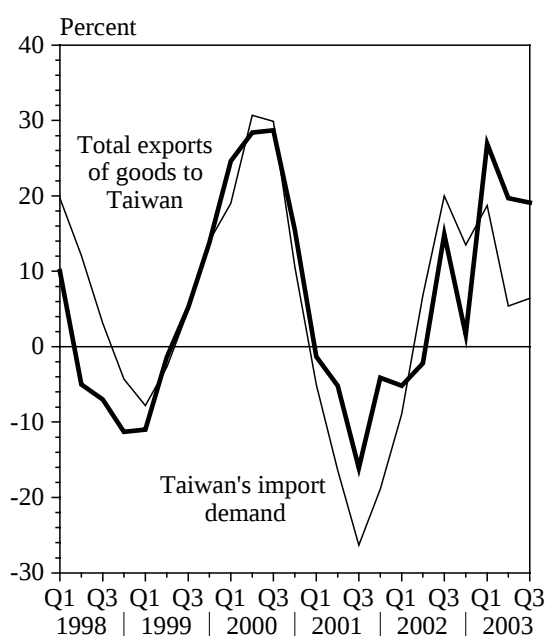
Note : (+) represents appreciation and (-) represents depreciation of the euro against HK\$.

/2.26

2.26 Total exports of goods to *Taiwan* remained buoyant in overall terms, with a further growth at 19.1% in real terms in the third quarter of 2003 over a year earlier, following an already robust growth at 23.2% in the first half of the year. For the first nine months of 2003 taken together, such exports surged by 21.7% in real terms over a year earlier. In particular, exports of material inputs to this market were vibrant in the third quarter. Exports of capital goods also had solid growth. But exports of consumer goods fell off, conceivably as import intake for consumption in Taiwan in the early part of the third quarter was still affected by the earlier shock of SARS.

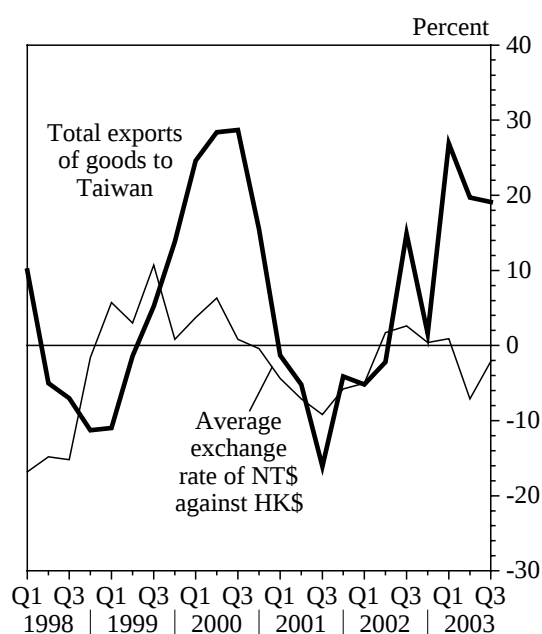
Diagram 2.16

**Total exports of goods to Taiwan
and Taiwan's import demand
(year-on-year rate of change)**



Note : See the footnote to Diagram 2.15.

**Total exports of goods to Taiwan
and the exchange rate factor
(year-on-year rate of change)**



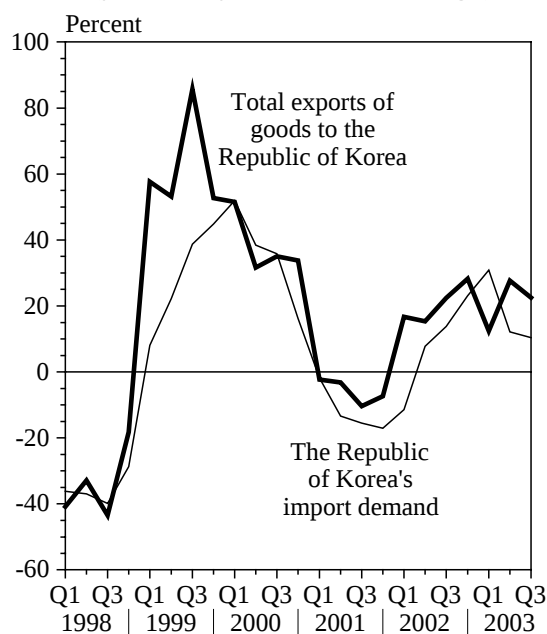
Note : (+) represents appreciation and (-) represents depreciation of the NT\$ against HK\$.

/2.27

2.27 Total exports of goods to the *Republic of Korea* continued to surge, by 22.5% in real terms in the third quarter of 2003 over a year earlier. Together with a 19.8% leap in the first half of the year, total exports of goods to this market soared by 20.8% in real terms in the first nine months of 2003 over a year earlier. The surge in the third quarter was particularly distinct growth in exports of capital goods and material inputs, in line with the robust performance of exports from that country. Exports of consumer goods also accelerated further in growth.

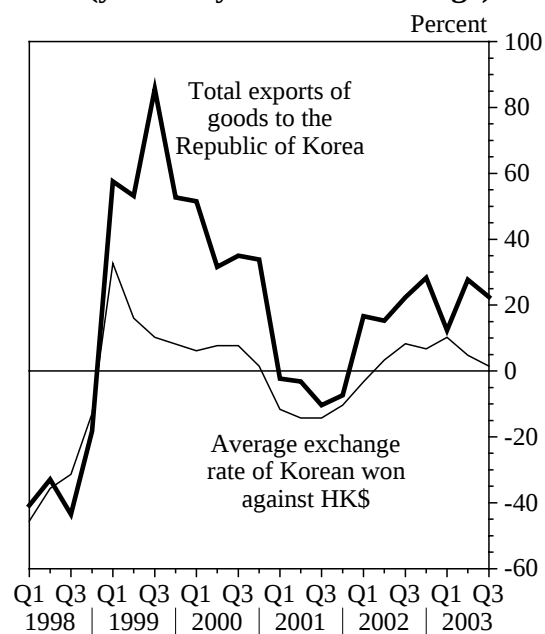
Diagram 2.17

Total exports of goods to the Republic of Korea and the Republic of Korea's import demand (year-on-year rate of change)



Note : See the footnote to Diagram 2.11.

Total exports of goods to the Republic of Korea and the exchange rate factor (year-on-year rate of change)



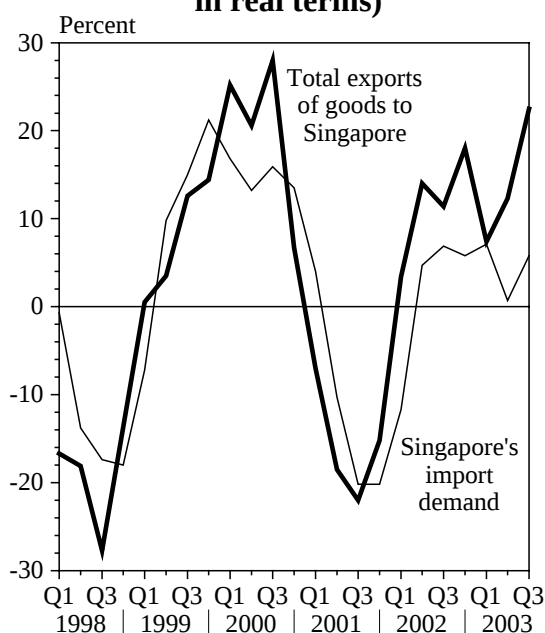
Note : (+) represents appreciation and (-) represents depreciation of the Korean won against HK\$.

/2.28

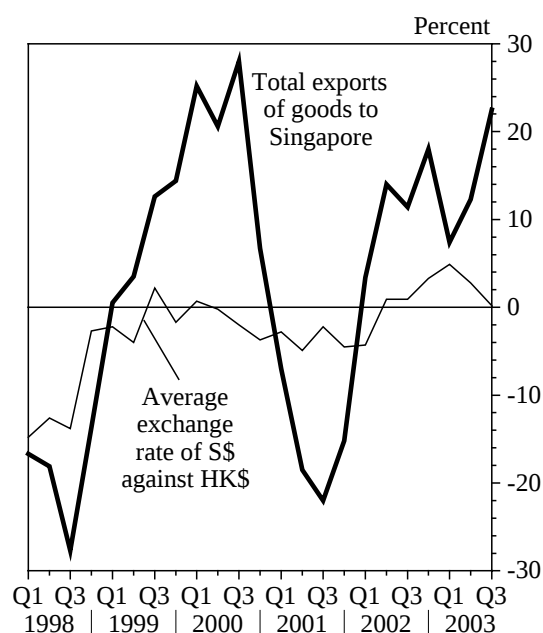
2.28 Total exports of goods to *Singapore* accentuated markedly further, to a 22.5% increase in real terms in the third quarter of 2003 over a year earlier. This gave a 14.4% gain in real terms in the first nine months of 2003 over a year earlier, after taking into account a 9.9% rise in the first half of the year. The lift in the third quarter was mainly led by a distinct surge in exports of capital goods, and to a lesser extent, by a pick-up in exports of consumer goods. Exports of material inputs also improved.

Diagram 2.18

Total exports of goods to Singapore and Singapore's import demand (year-on-year rate of change in real terms)



Total exports of goods to Singapore and the exchange rate factor (year-on-year rate of change)



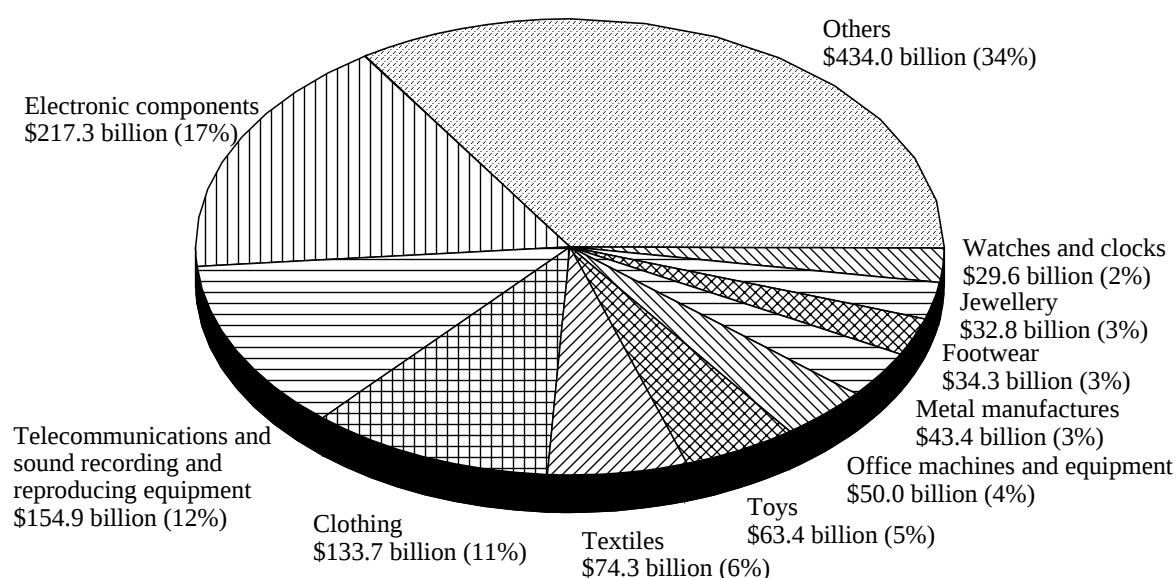
Note : (+) represents appreciation and (-) represents depreciation of the S\$ against HK\$.

/2.29

2.29 Analysed by major *commodity group*, electronic components continued to take up the largest share in Hong Kong's total exports of goods, at 17% of the total value in the first nine months of 2003. This was followed by telecommunications and sound recording and reproducing equipment (with a share of 12%), clothing (11%), textiles (6%), toys (5%), and office machines and equipment (4%). In the third quarter of 2003, exports of electronic components and of telecommunications products maintained highly distinct growth. Exports of office machines and equipment reverted to increase, having fallen for two consecutive quarters. On the other hand, owing to the setback in exports to the US market, exports of clothing rose only modestly, while exports of textiles and toys fell back by various degrees.

Diagram 2.19

**Total exports of goods by major commodity group
in the first nine months of 2003**



Total exports of goods in the first nine months of 2003 : \$1,267.6 billion

/Table 2.15

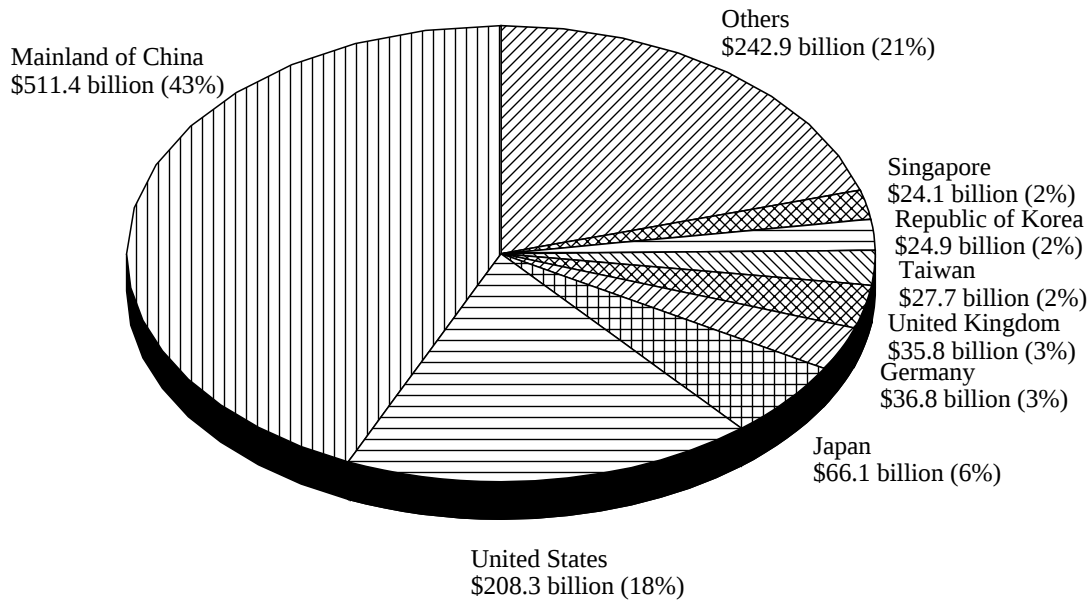
Table 2.15**Total exports of goods by major commodity group
(year-on-year rate of change in real terms (%))**

		<u>Electronic components</u>	<u>Telecom -munications and sound recording and reproducing equipment</u>	<u>Clothing</u>	<u>Textiles</u>	<u>Toys</u>	<u>Office machines and equipment</u>
2002	Annual	20.4	24.6	-1.1	5.5	1.4	31.1
	H1	9.4	10.7	-5.5	2.3	-5.2	36.4
	H2	30.9	36.3	2.4	8.6	6.0	26.4
	Q1	5.1	6.6	-7.7	-7.3	-12.6	37.8
	Q2	13.6	14.7	-3.6	10.3	1.5	35.0
	Q3	22.8	40.1	5.4	5.5	-1.8	18.7
	Q4	39.0	32.7	-0.9	11.9	17.5	33.9
2003	H1	39.3	33.7	5.5	7.1	7.9	-4.6
	Q1-Q3	39.2	27.2	3.7	2.6	2.8	-2.4
	Q1	37.2	37.2	9.6	16.2	10.0	-5.9
	Q2	41.2	30.4	1.9	0.8	6.3	-3.2
	Q3	39.2	18.3	1.3	-5.6	-3.1	2.0

Re-exports

2.30 Re-exports remained a predominant component over domestic exports within total exports of goods, with a share of 93% by value in the first nine months of 2003, further up from 91% in the same period in 2002. Analysed by major *market*, the Mainland took up the largest share in Hong Kong's re-exports, at 43% by value in the first nine months of 2003. The United States came next (with a share of 18%), followed by Japan (6%), Germany (3%), the United Kingdom (3%), Taiwan (2%), the Republic of Korea (2%), and Singapore (2%).

/Diagram 2.20

Diagram 2.20**Re-exports by major market in the first nine months of 2003**

Total re-exports in the first nine months of 2003 : \$1,178.1 billion

Table 2.16**Value of re-exports by market**

	2002			Jan-Sep 2003		
	Value (\$Bn)	Share in total (%)	Rate of change (%)	Value (\$Bn)	Share in total (%)	Year-on-year rate of change (%)
All markets	1,429.6	100	7.7	1,178.1	100	13.7
Mainland of China	571.9	40	15.2	511.4	43	23.7
United States	291.0	20	3.1	208.3	18	-1.8
Japan	80.7	6	-3.4	66.1	6	14.5
Germany	44.6	3	-2.6	36.8	3	18.6
United Kingdom	46.6	3	-0.3	35.8	3	5.9
Taiwan	30.2	2	0.6	27.7	2	25.4
Republic of Korea	29.3	2	18.8	24.9	2	17.9
Singapore	29.4	2	9.3	24.1	2	12.9
Rest of the world	305.8	21	5.1	242.9	21	8.8

/2.31

2.31 As the base of comparison back in 2002 shifted higher, the growth in re-exports to most of the major markets were not as fast in the third quarter of 2003 as in the second quarter. Even so, re-exports to many of the East Asian economies, including the Mainland, Singapore, the Republic of Korea and Taiwan, still maintained highly robust growth well in excess of 20% in the third quarter. Re-exports to Japan and Germany also held up well, both with a 14% growth. Re-exports to the United Kingdom had relatively steady growth, at 8%. Re-exports to the United States however slackened further, to a decline of 6%.

Table 2.17

**Re-exports by major market
(year-on-year rate of change in real terms (%))**

		<u>Mainland of China</u>	<u>United States</u>	<u>Japan</u>	<u>Germany</u>	<u>United Kingdom</u>	<u>Taiwan</u>	<u>Republic of Korea</u>	<u>Singapore</u>
2002	Annual	18.5	6.0	*	0.7	2.8	4.7	22.5	13.8
	H1	11.1	-2.6	-7.9	-8.4	-2.7	-3.8	18.2	12.0
	H2	25.1	13.5	7.6	8.6	7.4	13.2	26.7	15.4
	Q1	7.8	-12.2	-10.3	-13.7	-8.4	-6.0	19.5	7.1
	Q2	14.0	6.5	-5.3	-2.5	2.9	-1.7	16.8	17.2
	Q3	18.4	11.2	3.1	6.6	6.2	18.8	23.6	12.5
	Q4	32.5	16.1	12.1	10.4	8.7	8.2	29.7	18.1
2003	H1	28.6	4.6	17.6	27.6	8.6	33.4	21.0	10.4
	Q1-Q3	25.8	0.2	16.2	22.2	8.3	30.3	21.4	15.3
	Q1	32.3	12.2	16.0	28.4	8.2	37.3	13.4	8.2
	Q2	25.5	-1.2	19.2	26.9	8.8	29.8	29.0	12.5
	Q3	21.3	-6.1	13.7	13.8	8.0	25.0	22.1	24.3

Note : (*) Change of less than 0.05%.

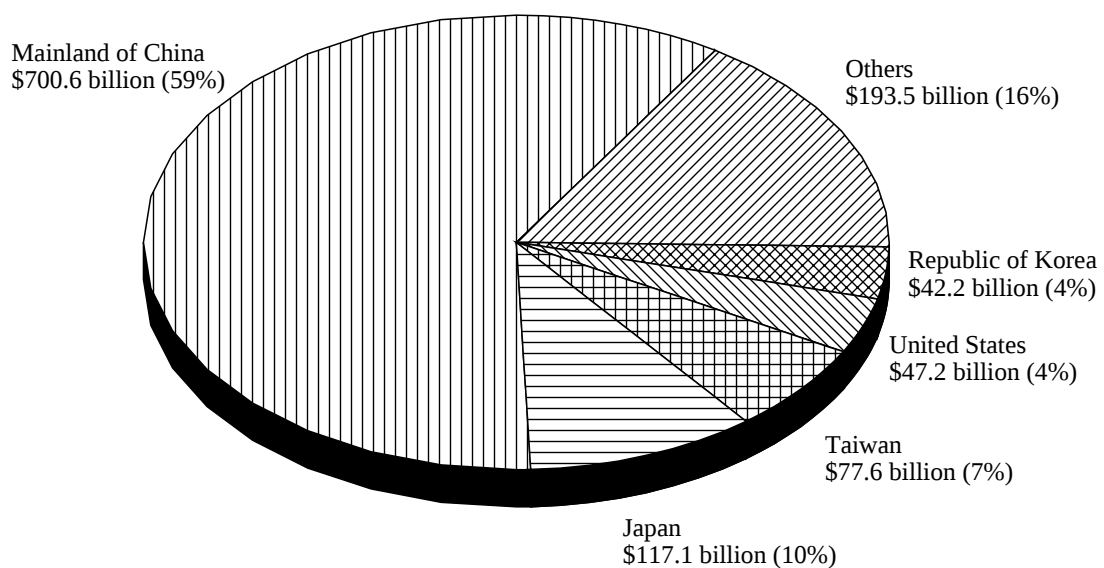
/2.32

2.32 The Mainland was still the largest *source* of Hong Kong's re-exports, supplying 59% by value of the goods re-exported through Hong Kong in the first nine months of 2003. This was followed by Japan (with a share of 10%), Taiwan (7%), the United States (4%), and the Republic of Korea (4%).

2.33 Re-exports sourced from most of the suppliers in East Asia maintained relatively rapid growth in the third quarter of 2003, with those sourced from Singapore being particularly distinct. Re-exports sourced from Germany held up better, but re-exports sourced from the United States slackened to decline.

Diagram 2.21

Re-exports by major source in the first nine months of 2003



Total re-exports in the first nine months of 2003 : \$1,178.1 billion

/Table 2.18

Table 2.18**Value of re-exports by source**

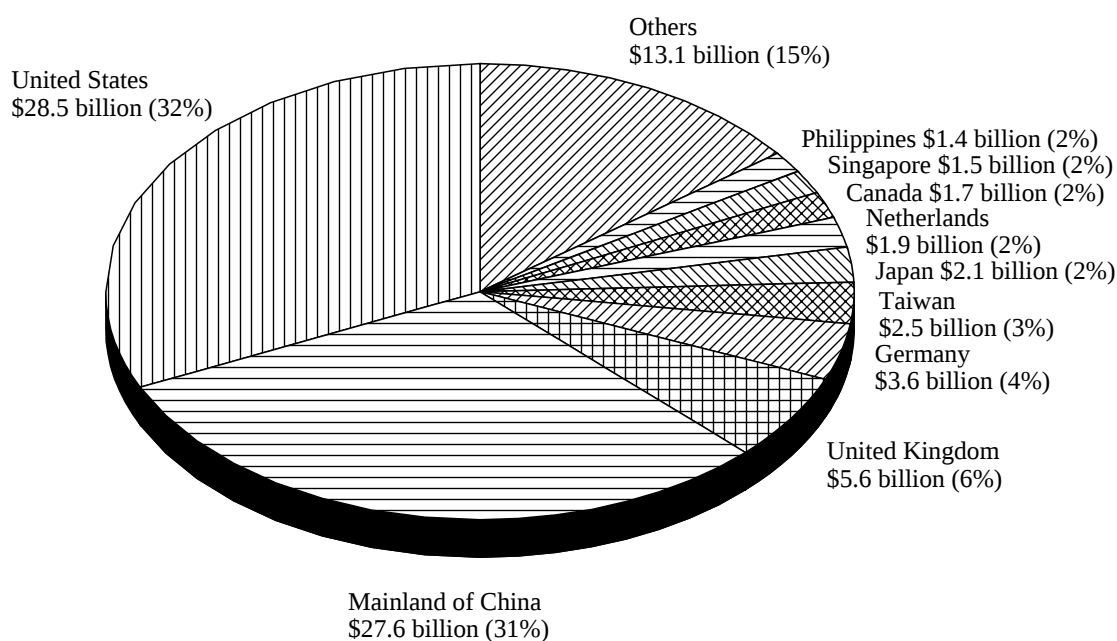
	<u>2002</u>			<u>Jan-Sep 2003</u>		
	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Rate</u> <u>of change</u> (%)	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Year-on-year</u> <u>rate of change</u> (%)
All sources	1,429.6	100	7.7	1,178.1	100	13.7
Mainland of China	864.0	60	6.9	700.6	59	12.4
Japan	135.8	9	8.1	117.1	10	19.4
Taiwan	94.3	7	17.4	77.6	7	13.4
United States	62.9	4	-3.5	47.2	4	1.1
Republic of Korea	47.2	3	18.7	42.2	4	23.8
Rest of the world	225.4	16	8.3	193.5	16	17.0

Domestic exports

2.34 The United States and the Mainland were the two largest *markets* for Hong Kong's domestic exports, accounting for 32% and 31 % respectively of the total value in the first nine months of 2003. Other significant markets were the United Kingdom (with a share of 6%), Germany (4%), Taiwan (3%), Japan (2%), the Netherlands (2%), Canada (2%), Singapore (2%), and the Philippines (2%).

2.35 Domestic exports to most of the major markets showed relative improvement in the third quarter of 2003, having been on a downslide during most of the first half of the year. In particular, domestic exports to Germany maintained highly distinct growth in the third quarter, while domestic exports to Japan picked up further in growth. The declines in domestic exports to the United States, the Mainland and Taiwan also narrowed significantly. On the other hand, domestic exports to the United Kingdom had a lesser rise, while domestic exports to Canada slackened to decline.

/Diagram 2.22

Diagram 2.22**Domestic exports by major market in the first nine months of 2003**

Total domestic exports in the first nine months of 2003 : \$89.6 billion

Table 2.19**Value of domestic exports by market**

	<u>2002</u>			<u>Jan-Sep 2003</u>		
	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Rate</u> <u>of change</u> (%)	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Year-on-year</u> <u>rate of change</u> (%)
All markets	130.9	100	-14.7	89.6	100	-8.9
United States	41.9	32	-11.9	28.5	32	-8.1
Mainland of China	41.4	32	-16.5	27.6	31	-13.7
United Kingdom	7.6	6	-11.5	5.6	6	4.5
Germany	4.3	3	-26.6	3.6	4	12.2
Taiwan	4.4	3	-17.9	2.5	3	-25.2
Japan	3.0	2	-26.9	2.1	2	-7.6
Netherlands	3.5	3	-24.9	1.9	2	-31.2
Canada	2.4	2	-22.0	1.7	2	-3.5
Singapore	2.2	2	-18.4	1.5	2	-5.1
Philippines	1.7	1	-7.0	1.4	2	8.6
Rest of the world	18.7	14	-8.4	13.1	15	-3.8

/Table 2.20

Table 2.20

**Domestic exports by major market
(year-on-year rate of change in real terms (%))**

		<u>United States</u>	<u>Mainland of China</u>	<u>United Kingdom</u>	<u>Germany</u>	<u>Taiwan</u>	<u>Japan</u>	<u>Netherlands</u>	<u>Canada</u>
2002	Annual	-9.5	-13.5	-10.2	-25.7	-11.4	-22.0	-4.5	-19.9
	H1	-15.2	-5.9	-22.8	-29.7	-3.1	-17.1	7.0	-28.9
	H2	-4.5	-20.3	1.0	-21.4	-19.1	-26.5	-16.2	-12.1
	Q1	-18.1	3.5	-22.8	-33.3	-0.8	-12.9	14.0	-24.7
	Q2	-12.7	-13.3	-22.7	-25.6	-5.3	-21.4	2.4	-32.4
	Q3	1.5	-19.1	-0.5	-17.6	-5.8	-27.2	-0.3	-22.5
	Q4	-10.9	-21.7	2.5	-25.0	-29.6	-25.7	-30.9	3.8
2003	H1	-15.3	-18.8	9.8	13.3	-32.3	-2.1	-45.0	6.3
	Q1-Q3	-11.9	-13.4	5.9	14.1	-28.8	0.5	-39.9	-0.3
	Q1	-9.1	-23.2	10.4	10.2	-27.7	-6.4	-34.2	6.3
	Q2	-20.3	-14.6	9.2	16.5	-36.9	2.7	-53.0	6.2
	Q3	-7.1	-2.9	0.7	15.6	-21.3	5.7	-28.5	-9.0

Box 2.2

Structural shift in Hong Kong's external trade

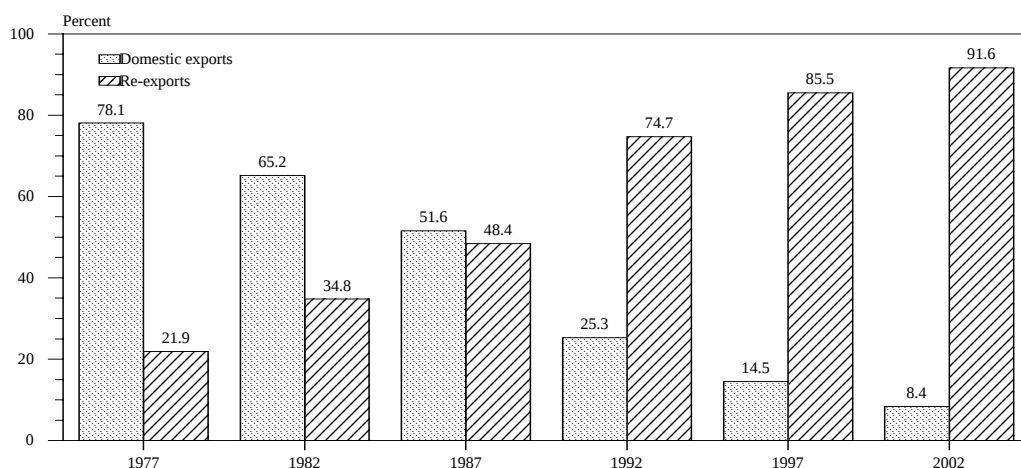
Hong Kong's merchandise trade has been undergoing substantial structural shift over the past two decades. In the 1970s, domestic exports took up a predominant share in Hong Kong's total exports of goods, at around 74-81% of the total value, while re-exports accounted for the remaining 19-26%. Following the Mainland's opening up in 1978, its exports have been expanding at a phenomenal pace. Hong Kong naturally re-emerged as the Mainland's key entrepôt, by virtue of its proximity to the Mainland, its extensive trading system, and its efficient physical infrastructure and support services. As a result, Hong Kong's merchandise trade underwent its first phase of structural shift from domestic exports to re-exports, with the share of re-exports in the value of total exports of goods rising distinctly, from slightly above 20% in the mid-1970s to around 35% in the early 1980s.

The structural shift towards re-exports accelerated further after the early part of the 1980s, this time prompted by the progressive relocation of production processes across the boundary to take advantage of the cheaper land and labour resources there. Throughout the period 1983-1995, re-exports attained uninterrupted double-digit growth, at an average annual rate of 24% in real terms. As a result, the share of re-exports in the value of total exports of goods leaped from 35% in 1983 to 83% in 1995 and further to 92% in 2002.

/Box 2.2 (cont'd)

Box 2.2 (cont'd)

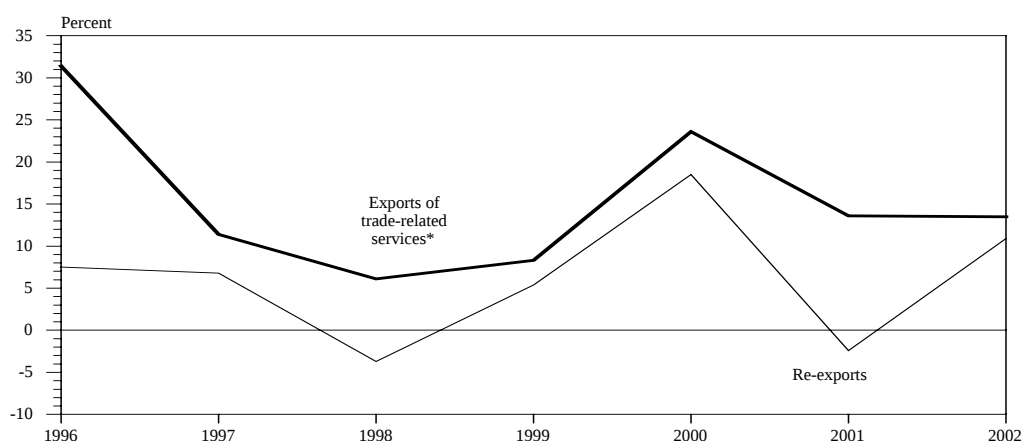
Composition of Hong Kong's total exports of goods



With the rapid development of port and other related infrastructural facilities and the streamlining of customs procedures in the Mainland, by around the mid-1990s a new trend of structural shift, whereby the finished products could be shipped out directly from the Mainland without passing through Hong Kong, had emerged. The yet further shift away from re-exports towards this newer shipping mode, known as offshore trade, represented the second phase of structural shift in Hong Kong's external trade.

Under the momentum of this second phase of structural shift, exports of trade-related services (comprising mainly offshore trade) persistently rose faster than re-exports in the more recent years, recording double-digit growth averaging at 15% in real terms in 1996-2002. This was also distinctly faster than the respective trend growth rate at only 5% in 1991-1995. In particular, even in the difficult years of 1998 and 2001, exports of trade-related services still registered notable growth, at 6% and 14% respectively. By contrast, re-exports had considerably slower growth, at an average annual rate of only 6% in real terms in 1996-2002. It was also markedly down from the respective trend growth rate at 20% in 1991-1995.

Exports of trade-related services vs re-exports
(growth rate in real terms)



Note : (*) Comprising mainly offshore trade.

Hence, as more and more of the shipments handled by Hong Kong companies go through the Mainland ports, rather than passing through the Hong Kong port as before, the growth momentum in Hong Kong's external trade has more recently been, and will continue to be, geared increasingly towards offshore trade.

/Outward

Outward processing trade

2.36 Outward processing trade⁽⁹⁾ remained an integral component in Hong Kong's overall merchandise trade. In the first half of 2003, 43% of Hong Kong's total exports of goods to the Mainland were for outward processing, as against 46% in the same period in 2002. In the first half of 2003, 69% of Hong Kong's imports of good from the Mainland were products after outward processing, as against 73% in the first half of 2002. As to re-exports of Mainland origin in the first half of 2003, 80% were products of outward processing, as against 84% in the first half of 2002.

2.37 While the proportion attributed to outward processing in Hong Kong's trade with the Mainland was down, this was merely a reflection of the rising importance of the Mainland economy as a market for Hong Kong's exports, in line with its robust domestic demand. Total exports of goods to the Mainland for outward processing were actually strong all through the first half of this year. There was a 20.4% surge in value terms in the second quarter of 2003 over a year earlier, even faster than the 13.6% rise in the first quarter. Continued buoyancy in the Mainland's own exports was the main contributory factor. For the first half of 2003 as a whole, these exports leaped by 17.3% in value terms over a year earlier to \$148.8 billion, up further from a 13.8% increase in the second half of 2002.

2.38 Total exports of goods to the Mainland for meeting its own demand continued on a sharp uptrend, with a 21.0% rise in value terms in the second quarter of 2003 over a year earlier, after a 39.0% surge in the first quarter. For the first half of 2003 as a whole, these exports soared by 29.2% in value terms over a year earlier to \$194.7 billion, up further from a 23.0% increase in the second half of 2002.

/Diagram 2.23

Diagram 2.23

**Exports to the mainland of China for outward processing and
for meeting its own demand
(year-on-year rate of change in value terms)**

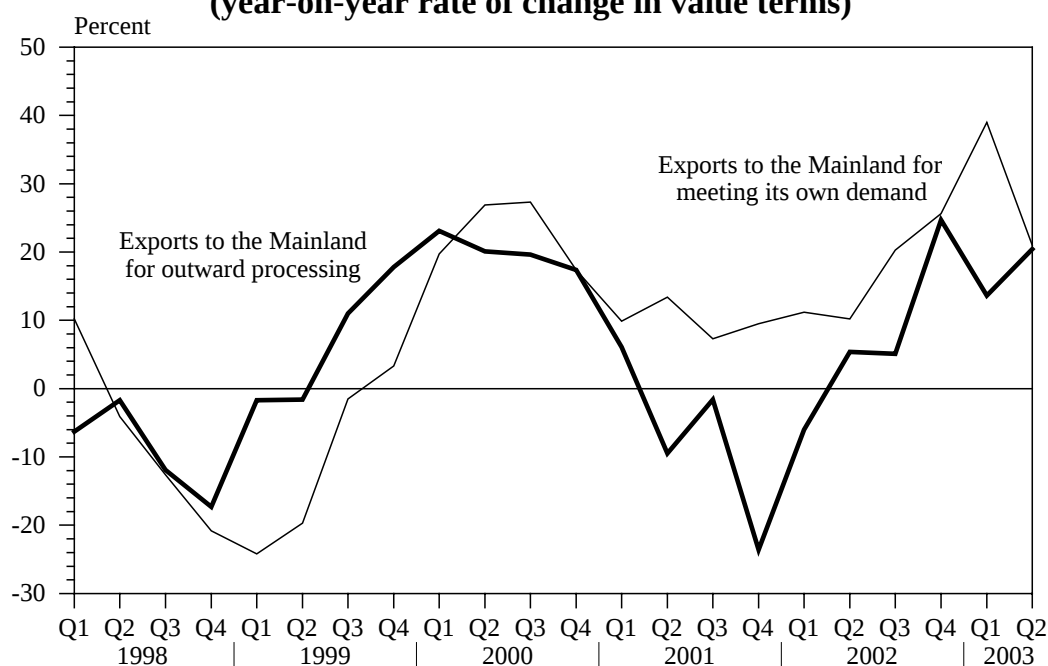


Table 2.21

**Total exports of goods to the mainland of China
for outward processing and for meeting its own demand
(year-on-year rate of change in value terms (%))**

Of which :

		Total exports of goods to the Mainland	Total exports of goods to the Mainland for outward processing	Total exports of goods to the Mainland for meeting its own demand
2002	Annual	12.3	7.0	17.1
	H1	5.4	-0.1	10.6
	H2	18.7	13.8	23.0
	Q1	2.6	-6.0	11.2
	Q2	7.9	5.4	10.2
	Q3	12.8	5.1	20.3
	Q4	25.2	24.7	25.6
2003	H1	23.8	17.3	29.2
	Q1	27.3	13.6	39.0
	Q2	20.8	20.4	21.0

/2.39

2.39 Imports of goods from the Mainland after outward processing picked up again to a 7.1% increase in value terms in the second quarter of 2003 over a year earlier, from a 5.4% rise in the first quarter. For the first half of 2003 as a whole, these imports rose by 6.3% in value terms over a year earlier to \$246.6 billion, following a 7.0% increase in the second half of 2002. Re-exports of Mainland origin after outward processing accentuated visibly in growth, to a 7.6% increase in value terms in the second quarter of 2003 over a year earlier, from a mere 0.1% increase in the first quarter. For the first half of 2003 as a whole, these re-exports reached \$276.7 billion, representing an increase of 4.0% over a year earlier. The respective growth in the second half of 2002 was higher, at 10.4%.

Table 2.22

**Imports of goods from the mainland of China
and re-exports of Mainland origin
to overseas markets after outward processing
(year-on-year rate of change in value terms (%))**

		<u>Imports of goods from the Mainland after outward processing</u>	<u>Re-exports of Mainland origin after outward processing</u>
2002	Annual	-0.2	2.8
	H1	-8.1	-5.2
	H2	7.0	10.4
	Q1	-9.0	-5.3
	Q2	-7.3	-5.0
	Q3	6.3	4.3
	Q4	7.8	17.2
2003	H1	6.3	4.0
	Q1	5.4	0.1
	Q2	7.1	7.6

Imports of goods

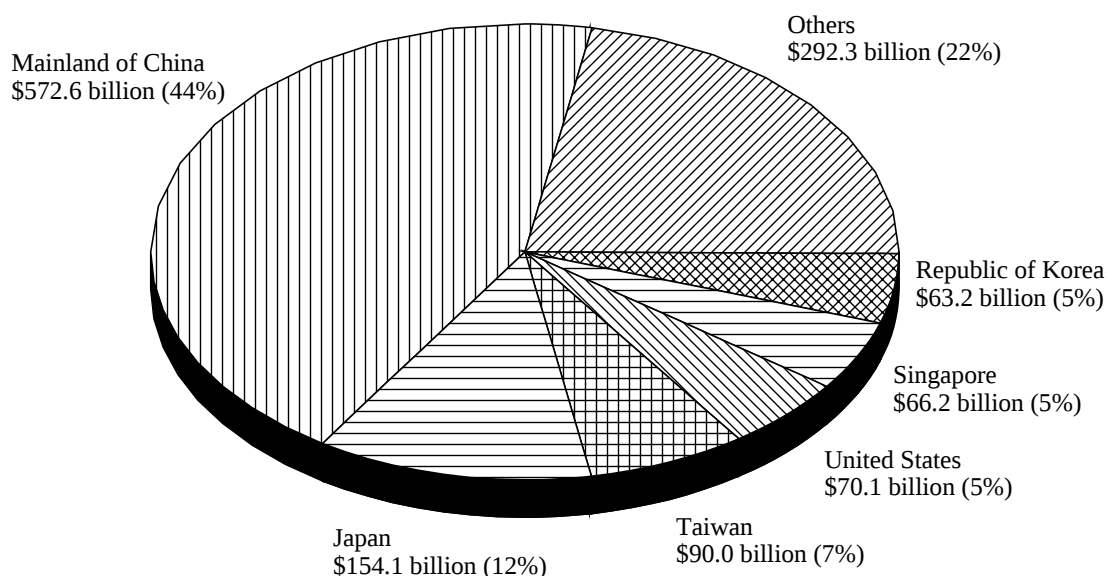
2.40 The Mainland remained the largest *source* of Hong Kong's imports of goods, taking up 44% of the total value in the first nine months of 2003. This was followed by Japan (with a share of 12%), Taiwan (7%), the United States (5%), Singapore (5%), and the Republic of Korea (5%).

/2.41

2.41 Imports from almost all major sources recorded further growth in the third quarter of 2003. But the year-on-year growth rates were generally more moderate than in the second quarter, due in large part to a higher base of comparison in the third quarter of 2002.

Diagram 2.24

**Imports of goods by major source
in the first nine months of 2003**



Total imports of goods in the first nine months of 2003 : \$1,308.5 billion

Table 2.23

Value of imports of goods by source

	<u>2002</u>			<u>Jan-Sep 2003</u>		
	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Rate</u> <u>of change</u> (%)	<u>Value</u> (\$Bn)	<u>Share</u> <u>in total</u> (%)	<u>Year-on-year</u> <u>rate of change</u> (%)
All sources	1,619.4	100	3.3	1,308.5	100	10.7
Mainland of China	717.1	44	5.1	572.6	44	9.8
Japan	182.6	11	3.4	154.1	12	17.3
Taiwan	115.9	7	7.4	90.0	7	6.0
United States	91.5	6	-12.8	70.1	5	3.1
Singapore	75.7	5	3.9	66.2	5	21.9
Republic of Korea	76.0	5	7.3	63.2	5	13.8
Rest of the world	360.7	22	2.2	292.3	22	9.7

/Table 2.24

Table 2.24

Imports of goods by major source
(year-on-year rate of change in real terms (%))

		<u>Mainland of China</u>	<u>Japan</u>	<u>Taiwan</u>	<u>United States</u>	<u>Singapore</u>	<u>Republic of Korea</u>
2002	Annual	9.0	7.7	12.0	-7.9	10.0	12.5
	H1	3.1	-3.0	3.3	-14.4	1.3	1.1
	H2	14.2	18.8	20.8	-1.2	18.5	24.3
	Q1	-2.7	-7.4	1.0	-16.4	-1.0	-3.1
	Q2	8.6	1.2	5.4	-12.5	3.4	5.2
	Q3	11.9	12.7	16.9	-8.0	9.8	24.6
	Q4	16.7	25.2	25.0	6.7	27.9	24.1
2003	H1	12.8	16.5	7.7	8.2	27.8	18.1
	Q1-Q3	10.4	14.5	6.6	6.3	26.3	19.8
	Q1	15.9	23.1	11.7	10.7	31.0	18.7
	Q2	10.3	10.8	4.3	6.0	24.8	17.5
	Q3	6.5	11.0	4.8	2.8	23.9	22.8

Retained imports

2.42 Japan continued to be the largest *source* of Hong Kong's retained imports, taking up about 16% of the total value in the first nine months of 2003. Other more significant suppliers of retained imports were the Republic of Korea (with a share of 10%), the Mainland (8%), Singapore (8%), the United States (7%), and Taiwan (5%).

2.43 Analysed by *end-use category*, retained imports of consumer goods turned up to a 3.2% increase in real terms in the third quarter of 2003 over a year earlier, as demand for these goods gradually recovered after the earlier setback caused by SARS. With a 2.2% decline in the first half of the year, retained imports of consumer goods still fell marginally, by 0.2% in real terms in the first nine months of 2003 over a year earlier. Retained imports of foodstuffs likewise reverted to increase, albeit only slightly, rising by 1.5% in real terms in the third quarter of 2003 over a year earlier. This, together with a 5.4% slump in the first half of the year, gave a 3.1% decline in real terms in the first nine months of 2003 over a year earlier.

/2.44

2.44 Retained imports of capital goods also resumed increase after the dip in the second quarter, albeit aided in part by the intake of aircraft ordered earlier. There was a moderate increase by 5.1% in real terms in the third quarter of 2003 over a year earlier. This, combined with a 3.5% rise in the first half of the year, yielded a 4.1% growth in real terms in the first nine months of 2003 over a year earlier. Analysed by broad type, intake of telecommunications equipment accentuated distinctly in growth in the third quarter, while intake of office equipment rebounded to a modest rise. On the other hand, intake of both industrial machinery and construction machinery and of capital goods in the “others” category remained weak.

2.45 Retained imports of raw materials and semi-manufactures receded to decline, by 6.7% in real terms in the third quarter of 2003 over a year earlier, having recorded positive growth for five consecutive quarters. Together with an 11.2% surge in the first half of the year, these retained imports rose by 4.6% in real terms in the first nine months of 2003 over a year earlier. Retained imports of fuels turned up to a 0.6% increase in real terms in the third quarter of 2003 over a year earlier, having fallen by 2.7% in the first half of the year. This resulted in a 1.5% decline in real terms in the first nine months of 2003 over a year earlier.

Table 2.25

**Retained imports by end-use category
(year-on-year rate of change in real terms (%))**

		<u>Consumer goods</u>	<u>Foodstuffs</u>	<u>Capital goods</u>	<u>Raw materials and semi-manufactures</u>	<u>Fuels</u>
2002	Annual	5.7	5.3	-13.6	9.8	4.8
	H1	0.7	9.7	-16.6	-2.1	0.7
	H2	10.7	1.2	-10.9	23.1	8.8
	Q1	-2.3	14.2	-23.0	-9.2	-3.3
	Q2	3.3	5.0	-10.1	4.4	4.4
	Q3	11.9	-8.9	-18.0	27.1	7.8
	Q4	9.3	12.7	-2.3	19.1	9.7
2003	H1	-2.2	-5.4	3.5	11.2	-2.7
	Q1-Q3	-0.2	-3.1	4.1	4.6	-1.5
	Q1	7.7	-4.6	10.6	18.0	9.1
	Q2	-10.3	-6.2	-2.8	5.9	-12.8
	Q3	3.2	1.5	5.1	-6.7	0.6

Note : See Note (a) to Table 2.7.

/Table 2.26

Table 2.26**Retained imports of capital goods by broad type
(year-on-year rate of change in real terms (%))**

		<u>Industrial machinery for manufacturing use</u>	<u>Construction machinery</u>	<u>Office equipment</u>	<u>Tele- communications equipment</u>	<u>Other capital goods</u>
2002	Annual	-1.5	11.1	-12.3	-2.5	-38.9
	H1	-6.0	14.7	-22.9	-10.5	-30.9
	H2	3.0	7.7	-2.4	6.1	-44.9
	Q1	-7.5	2.2	-43.5	-4.3	-36.2
	Q2	-4.6	25.3	1.0	-16.7	-25.2
	Q3	-5.3	19.8	-18.5	12.7	-50.0
	Q4	12.1	-3.3	21.0	-0.5	-38.2
2003	H1	-2.3	-16.6	19.6	-6.5	8.7
	Q1-Q3	-4.2	-20.7	12.9	6.8	3.8
	Q1	3.9	-9.4	52.9	-12.9	16.0
	Q2	-7.6	-21.6	-2.0	1.1	2.1
	Q3	-7.9	-28.6	2.9	29.3	-5.0

Note : See Note (a) to Table 2.7.

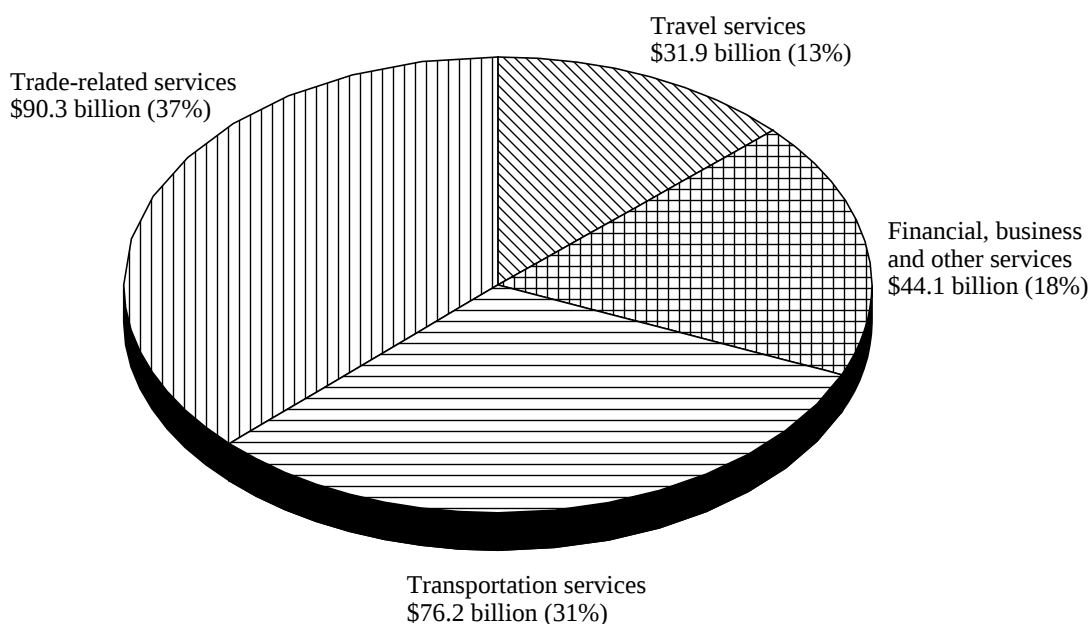
Invisible trade***Exports of services***

2.46 Trade-related services (comprising mainly offshore trade) continued to take up the largest share in Hong Kong's exports of services, at 37% by value in the first three quarters of 2003. Exports of transportation services came next (with a share of 31%), followed by exports of financial, business and other services (18%), and exports of travel services (13%).

/Diagram 2.25

Diagram 2.25

**Exports of services by major service group
in the first three quarters of 2003**



Exports of services in the first three quarters of 2003 : \$242.6 billion

2.47 Exports of services reverted to increase, up by 6.9% in real terms in the third quarter of 2003 over a year earlier, after an abrupt fall-off by 13.9% in the second quarter upon the outbreak of SARS. For the first three quarters of 2003 as a whole, there was a modest growth at 1.9% in real terms over a year earlier.

2.48 The distinct turnaround in exports of services in the third quarter was marked by a progressive return of inbound tourism, particularly in respect of Mainland visitors, as the SARS impact waned. This was additionally boosted by the launch of the “individual visit” scheme for Mainland visitors to Hong Kong since late July. As incoming tourists came back swiftly, exports of travel services rebounded strongly to growth at 4.3% in real terms in the third quarter of 2003, from a sharp plunge of 71.4% in the second quarter. Transportation services also showed a relative improvement, yet not so prominently. While air passenger services resumed growth in the third quarter, sea freight services were dampened by a further fall-off in exports to the United States in that quarter. Overall, exports of transportation services were virtually unchanged in real terms in the third quarter of 2003 over a year earlier, much improved from the 14.6% dip in the second quarter.

/2.49

2.49 Exports of trade-related services, comprising mainly offshore trade, remained buoyant, rising by 13.9% in real terms in the third quarter of 2003 over a year earlier, having leaped by 15.0% in the second quarter. Continued surge in the Mainland's external trade was the main factor underpinning this strong uptrend. As to exports of financial, business and other services, they also promptly regained growth, at 5.4% in real terms in the third quarter of 2003 over a year earlier, as against a modest fall by 1.7% in the second quarter.

Table 2.27

**Exports of services by major service group[^]
(year-on-year rate of change in real terms (%))**

Of which :

		Exports of services	Trade-related services ^(a)	Transportation services	Travel services ^(b)	Financial, business and other services
2002	Annual	12.2	13.5	11.5	27.8	-0.7
	H1	7.7	7.9	6.6	19.1	0.9
	H2	16.1	17.7	16.3	36.1	-2.2
	Q1	6.3	7.1	6.7	10.9	1.4
	Q2	9.1	8.7	6.5	26.4	0.3
	Q3	14.0	16.5	15.4	29.1	-3.5
	Q4	18.1	18.8	17.2	42.3	-0.9
2003	H1	-1.0	17.6	-3.4	-31.2	-0.1
	Q1-Q3	1.9	16.0	-2.2	-18.9	1.7
	Q1	12.5	20.1	8.7	19.5	1.5
	Q2	-13.9	15.0	-14.6	-71.4	-1.7
	Q3	6.9	13.9	*	4.3	5.4

Notes : (^) Revised series after incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003. For details, see Box 1.1 in Chapter 1.

(a) Comprising mainly offshore trade.

(b) Comprising mainly inbound tourism receipts.

(*) Change of less than 0.05%.

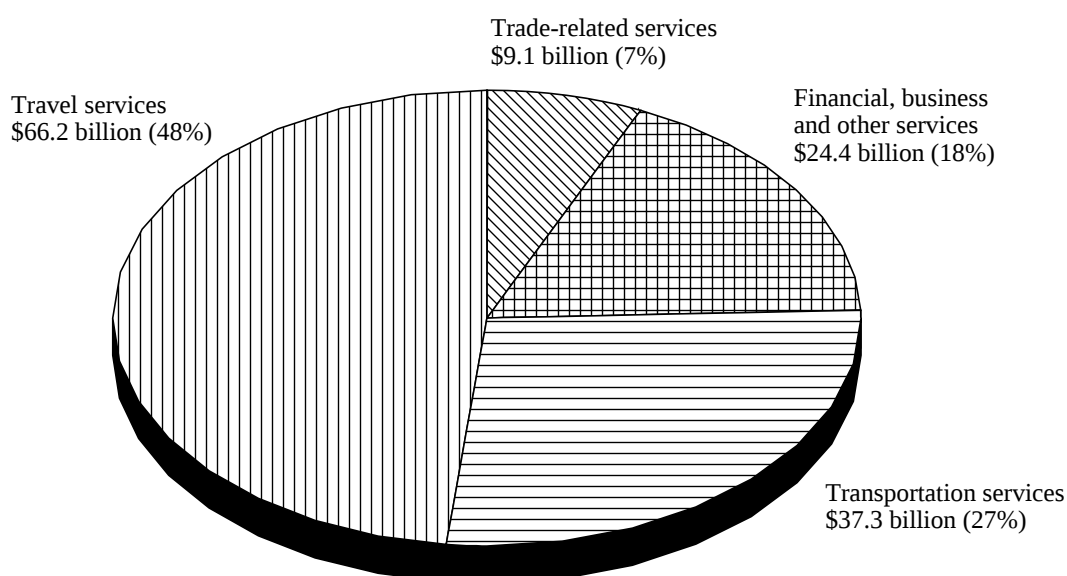
/Imports

Imports of services

2.50 Travel services continued to take up the largest share in Hong Kong's imports of services, at 48% by value in the first three quarters of 2003. This was followed by imports of transportation services (with a share of 27%), imports of financial, business and other services (18%), and imports of trade-related services (7%).

Diagram 2.26

Imports of services by major service group in the first three quarters of 2003



Imports of services in the first three quarters of 2003 : \$137.0 billion

2.51 As with exports of services, imports of services also staged a rebound in the third quarter of 2003, albeit up only marginally by 0.5% in real terms over a year earlier, after plummeting by 19.6% in the second quarter. There was still a 7.3% decline in real terms for the first three quarters of 2003 as a whole over a year earlier, owing to the severe setback caused by SARS in the second quarter.

2.52 The rebound in imports of services in the third quarter resembled that in exports of services, with a distinct turnaround in travel and related passenger transportation services after the SARS impact. As the arrival restrictions and post-arrival quarantine by some of the neighbouring places were lifted, and as

/local

local residents' inclination to go abroad was resurrected, the decline in real terms in residents' travel spending abroad narrowed significantly to 0.1% in the third quarter of 2003 over a year earlier, from a plunge of 29.1% in the second quarter. Imports of transportation services also improved, with the decline in real terms narrowed from 17.6% in the second quarter to 0.4% in the third quarter. Likewise, this was mostly driven by revival in air passenger services. Sea freight services remained on a decline, amidst subdued imports for local use for most of the quarter.

2.53 Imports of trade-related services continued to show solid growth, at 7.1% in the third quarter of 2003 over a year earlier, albeit slightly down from that of 8.1% in the second quarter. Meanwhile, imports of financial, business and other services reverted to increase, rising by 0.9% in real terms in the third quarter of 2003 over a year earlier, from a 4.6% decline in the second quarter.

Table 2.28

**Imports of services by major service group
(year-on-year rate of change in real terms (%))**

		<i>Of which :</i>				
		<u>Imports of services</u>	<u>Travel services^(a)</u>	<u>Transportation services</u>	<u>Trade-related services</u>	<u>Financial, business and other services</u>
2002	Annual	0.2	-0.5	2.8	6.8	-3.7
	H1	-2.2	-1.9	-3.4	1.4	-2.6
	H2	2.7	0.9	9.1	10.6	-4.6
	Q1	-0.7	0.1	-2.0	0.7	-1.8
	Q2	-3.8	-4.1	-4.7	2.2	-3.3
	Q3	2.0	1.0	6.8	9.5	-5.4
	Q4	3.4	0.8	11.7	11.7	-3.9
2003	H1	-11.5	-18.9	-7.4	10.5	-2.3
	Q1-Q3	-7.3	-12.5	-4.8	9.1	-1.2
	Q1	-3.9	-10.1	3.7	12.9	*
	Q2	-19.6	-29.1	-17.6	8.1	-4.6
	Q3	0.5	-0.1	-0.4	7.1	0.9

Notes : (a) Comprising mainly outbound travel spending.

(*) Change of less than 0.05%.

/Overall

Overall balance of payments⁽¹⁰⁾

2.54 The current account surplus dwindled markedly, to \$16.6 billion in the second quarter of 2003, equivalent to 5.8% of GDP in that quarter. The surplus was \$31.5 billion in the first quarter, equivalent to 10.6% of GDP in that quarter. The spread of SARS in the second quarter resulted in a distinct setback in inbound tourism and related service exports, and hence a shrinkage in the invisible trade surplus. A considerable contraction in net external factor income inflow in that quarter also mattered. These more than offset a reduction in the visible trade deficit, amidst the robust performance of merchandise exports in the same quarter.

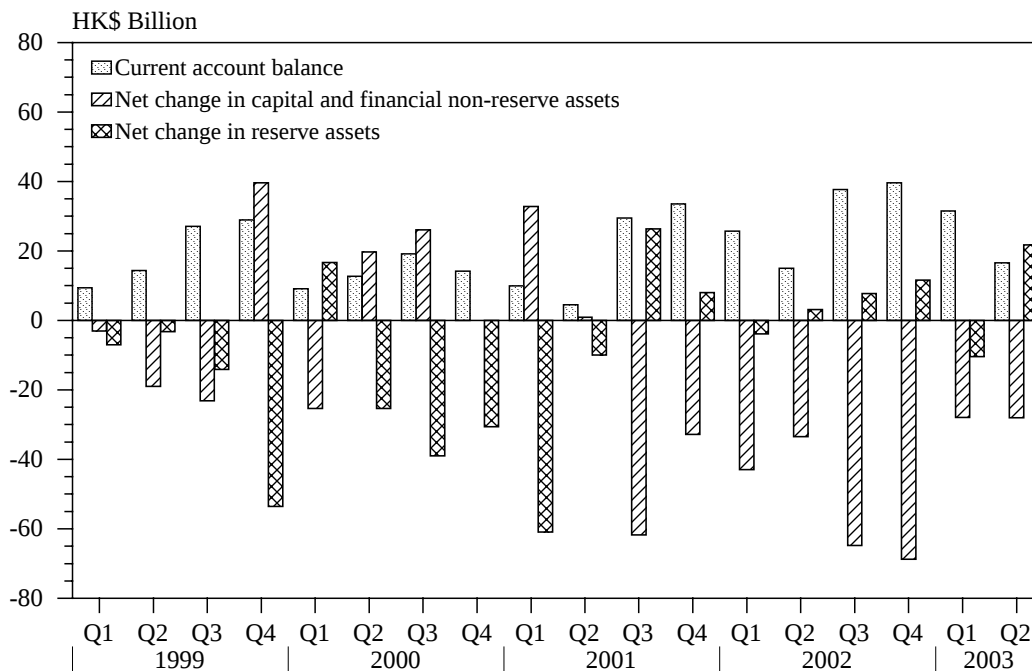
2.55 In the capital and financial account, there was a substantial net inflow of \$34.8 billion in the direct investment account in the second quarter, being the combined result of reduced direct investment abroad from Hong Kong and increased foreign direct investment into Hong Kong. Also, there was a significant net inflow of \$22.0 billion due to cash settlement of financial derivatives in the second quarter. Yet against these, the portfolio investment account recorded a considerable net outflow of \$25.9 billion in the second quarter, as Hong Kong investors increased their holdings of overseas debt securities while overseas investors concurrently reduced their holdings of local debt securities. Moreover, the other investment account switched sharply to net outflow at \$56.2 billion in the second quarter, upon decreases in currency and deposit liabilities of the local banking sector. Taken together, financial non-reserve assets recorded a net outflow of \$25.2 billion in the second quarter of 2003, equivalent to 8.7% of GDP in that quarter. This was slightly smaller than the corresponding net outflow of \$26.0 billion in the first quarter, equivalent to 8.7% of GDP in that quarter.

2.56 With the markedly reduced surplus on the current account being unable to offset the continued net outflow of funds in the capital and financial account, the overall balance of payments account receded to deficit at \$21.7 billion in the second quarter of 2003, equivalent to 7.5% of GDP in that quarter. Thus there was a corresponding decrease in reserve assets by the same amount in that quarter. This came after a surplus of \$10.4 billion in the first quarter, equivalent to 3.5% of GDP in that quarter.

/Diagram 2.27

Diagram 2.27

Major balances in Hong Kong's balance of payments



Note : A negative value for net change in reserve assets represents a net increase, and a positive value represents a net decrease.

Box 2.3

Effect of new tourism expenditure data on the balance of payments statistics

Balance of payments (BoP) measures the economic transactions of the Hong Kong economy with the rest of the world. Expenditure by non-residents in Hong Kong is classified as travel credit of the trade in services account under the current account of BoP. A change to the tourism expenditure data will lead to the same change in absolute amount in the balance of trade in services, and hence also the same change in absolute amount in the current account balance. Nevertheless, the overall BoP balance, being the exact mirror image of the change in official reserves which is ascertained from a separate source, will be totally unaffected. Yet a parallel adjustment, to the same absolute amount as with the change in the current account balance but in the opposite direction, will be made to net errors and omissions in the BoP account.

With the new set of data on destination consumption expenditure of incoming visitors and travellers (see the technical explanation in **Box 1.1** in Chapter 1) leading to lower exports of services, the surplus on trade in services is revised down to \$115.2 billion in 2001 and \$144.5 billion in 2002. Thus the current account surplus is also revised down, to \$77.5 billion in 2001 and \$118.1 billion in 2002, corresponding to 6.1% and 9.4% of GDP in those two years.

/Table 2.29

Table 2.29

Hong Kong's balance of payments account
(\$ billion at current market prices)

	<u>2001[#]</u>	<u>2002[#]</u>	<u>2002</u>				<u>2003</u>	
			<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>
Current account^(a)	77.5	118.1	25.7	15.0	37.7	39.6	31.5	16.6
Trade in goods	-65.0	-39.4	-12.4	-16.4	-5.0	-5.6	-16.0	-9.8
Trade in services	115.2	144.5	26.9	32.9	38.4	46.4	35.7	28.3
External factor income flows	41.2	27.4	14.8	2.1	8.1	2.4	15.9	1.5
Current transfers	-13.9	-14.5	-3.5	-3.6	-3.8	-3.6	-4.1	-3.5
Capital and financial account	-97.4	-191.4	-46.8	-30.4	-57.1	-57.2	-38.4	-6.3
Net change in capital transfers	-9.2	-15.7	-3.0	-7.6	-1.9	-3.2	-1.9	-2.8
Net change in financial non-reserve assets	-51.7	-194.2	-39.9	-25.9	-62.8	-65.5	-26.0	-25.2
<i>of which :</i>								
Direct investment	96.9	-31.0	-10.1	15.3	-32.7	-3.4	3.0	34.8
Portfolio investment	-322.0	-290.7	7.1	-117.8	-82.5	-97.6	-54.8	-25.9
Financial derivatives	39.6	10.6	12.3	6.1	-5.7	-2.0	12.1	22.0
Other investment	133.8	116.9	-49.2	70.6	58.1	37.5	13.6	-56.2
Net change in reserve assets ^(b)	-36.5	18.5	-3.9	3.1	7.7	11.6	-10.4	21.7
Net errors and omissions	19.8	73.3	21.1	15.3	19.4	17.6	6.9	-10.3
Overall balance of payments	36.5	-18.5	3.9	-3.1	-7.7	-11.6	10.4	-21.7

Notes : (#) Revised figures after incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003. For details, see Box 1.1 in Chapter 1.

(a) According to the international statistical standard for compiling balance of payments (BoP) account, imports of goods are valued on free-on-board (f.o.b.) basis, which is different from the practice for merchandise trade statistics where imports are valued on cost, insurance and freight (c.i.f.) basis. In the BoP account, the insurance and freight costs related to merchandise imports are entered as imports of services.

(b) A negative value for net change in reserve assets represents a net increase, and a positive value represents a net decrease.

/Notes

Notes :

- (1) Estimates of price changes for the trade aggregates are based on changes in unit values, which do not take into account changes in the composition or quality of the goods traded, except for some selected commodities for which specific price indices are available. Changes in real terms are derived by discounting the effect of price changes from changes in the value of the trade aggregates.
- (2) Re-exports are those goods which have previously been imported into Hong Kong and are subsequently exported without having undergone in Hong Kong any manufacturing processes which change permanently the shape, nature, form or utility of the goods.
- (3) Offshore trade is covered in exports of trade-related services within the broader component of exports of services in the Gross Domestic Product. It covers the services of both “merchanting” and “merchandising for offshore transactions”. Merchanting is defined as the services associated with trading of goods which are purchased from a party outside Hong Kong and then sold to another party outside Hong Kong, without the goods ever entering and leaving Hong Kong. Merchandising for offshore transactions is defined as the services of arranging on behalf of buyers/sellers outside Hong Kong the purchase/sale of goods according to their specifications. Earnings from offshore trade include the gross margin from merchanting and the commission from merchandising for offshore transactions.
- (4) Here imports of goods are valued on free-on-board (f.o.b.) basis, which is different from the practice for merchandise trade statistics where imports are valued on cost, insurance and freight (c.i.f.) basis. The insurance and freight costs related to merchandise imports are entered as imports of services.
- (5) Exports of financial and banking services in the GDP account include commissions and fees for rendering financial and related ancillary services to non-residents. However, these do not include interest receipts from non-residents, which account for a major part of the external receipts of financial intermediaries in Hong Kong. Interest receipts from non-residents are correctly classified as investment income from abroad under GNP. The same situation applies, in an opposite direction, to interest payments to non-residents. Hence the trade in services component and the invisible trade surplus of Hong Kong would have been larger if such interest receipts and payments were classified to the services account.
- (6) East Asia here covers nine major markets in the region, namely the mainland of China, Japan, Taiwan, Singapore, the Republic of Korea, the Philippines, Thailand, Malaysia and Indonesia.
- (7) North America here comprises the United States and Canada.

/(8)

- (8) There are currently 15 member countries in the European Union, namely the United Kingdom, Germany, the Netherlands, France, Sweden, Italy, Denmark, Spain, Finland, Belgium, Luxembourg, Ireland, Austria, Greece and Portugal.
- (9) Outward processing arrangements are made between Hong Kong companies and manufacturing entities in the Mainland under which the companies concerned sub-contract the whole or part of the production processes relating to their products to the Mainland entities. Raw materials or semi-manufactures are normally exported to the Mainland for such processing. The Mainland entity involved can be a local enterprise, a joint venture, or some other forms of business involving foreign investment.

There is no restriction on outward processing activities in general. However, outward processing on goods which claim Hong Kong origin status is strictly governed by the Hong Kong origin rules. The Trade and Industry Department operates an effective administrative arrangement whereby goods manufactured in Hong Kong but having undergone outward processing activities can be conferred Hong Kong origin status subject to the Hong Kong origin rules being fully met.

- (10) A balance of payments (BoP) account is a statistical framework that systematically summarises the external transactions of an economy with the rest of the world in a specific time period.

A complete BoP account comprises the current account and the capital and financial account. The current account records the flows of real resources, including exports and imports of goods and services, factor income received from and paid to abroad, and current transfers from and to abroad. The capital account records external capital transfers, and external acquisitions and disposals of non-produced and non-financial assets. The financial account records transactions in financial assets and liabilities between residents and non-residents, including direct investment, portfolio investment, financial derivatives, and other investment. Also included is net change in reserve assets.

Within the overall BoP account, the current account balance and the net change in capital and financial non-reserve assets taken together, which is deemed to represent the BoP position of the economy, matches exactly the net change in reserve assets, by virtue of the BoP accounting identity.

CHAPTER 3 : THE DOMESTIC ECONOMY

Net output or value added by major economic sector

3.1 As reflected in quarterly GDP by major economic sector at constant prices⁽¹⁾, net output or value added for all the *service sectors* taken together⁽²⁾ rose by only 0.6% in real terms in the second quarter of 2003 over a year earlier, distinctly slower than the 5.6% increase in the first quarter. Analysed by constituent sector and in real terms, net output in transport, storage and communications decreased by 6.5% in the second quarter of 2003 over a year earlier. This was mainly attributable to the setback in air and land transport services amidst the SARS impact. Yet sea transport services held up well, underpinned by buoyancy in external trade. Also, there was a further expansion in communication services. Net output in community, social and personal services decreased by 3.6%. This was mainly due to the decline in recreation and entertainment services upon the spread of SARS. On the other hand, net output in the wholesale, retail and import/export trades, restaurants and hotels increased by 5.8%. The strong increase in net output in the import/export trade more than offset the significant declines, owing to the SARS impact, in net output in the wholesale and retail trades and in restaurants and hotels. Net output in financing, insurance, real estate and business services rose by 1.6%. It mainly came from improved performance of banking services. Also relevant was buoyancy in stock brokerage, along with a distinctly larger stock market turnover.

3.2 Net output in the local *manufacturing sector* shrank distinctly further, by 12.5% in real terms in the second quarter of 2003 from a year earlier, after an 8.8% decrease in the first quarter. Sluggish performance of domestic exports largely contributed. As to the *construction sector*, net output declined by 7.0% in real terms in the second quarter of 2003 from a year earlier, following a 3.2% decrease in the first quarter. This was mainly due to winding down of some major infrastructural projects and slack building activity.

/Table 3.1

Table 3.1

GDP by major economic sector^(a)
(year-on-year rate of change in real terms (%))

		<u>2002[#]</u>				<u>2003[#]</u>	
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
Manufacturing	-9.8	-11.6	-11.2	-7.3	-9.2	-8.8	-12.5
Construction	-1.0	-1.7	3.2	2.4	-6.4	-3.2	-7.0
Services ^(b)	3.1	*	1.5	4.3	6.4	5.6	0.6
<i>Of which :</i>							
Wholesale, retail and import/export trades, restaurants and hotels	5.1	-2.8	0.5	6.9	14.5	14.4	5.8
Transport, storage and communications	4.0	0.2	3.6	5.5	6.2	3.8	-6.5
Financing, insurance, real estate and business services	0.9	-1.5	0.9	1.6	2.5	2.7	1.6
Community, social and personal services	0.7	1.0	0.3	1.1	0.5	-0.4	-3.6

Notes : (a) The GDP figures shown in this table are compiled from the production approach, in parallel with those shown in Table 1.1 which are compiled from the expenditure approach. For details, see Note (1) to this chapter.

(b) In the context of value added contribution to GDP, the service sectors include ownership of premises as well, which is analytically a service activity. Also, charges of financial intermediation services are deducted.

(#) Revised figures.

(*) Change of less than 0.05%.

/Local

Local manufacturing output

3.3 The Index of Industrial Production⁽³⁾, as also reflecting output volume in the local manufacturing sector, declined distinctly further, by 12.5% in the second quarter of 2003 over a year earlier, after an 8.8% decline in the first quarter. Analysed by major constituent industry and in volume, output of the machinery and equipment and the fabricated metal products industries plunged the most, by 30.4% and 21.5% respectively in the second quarter of 2003 over a year earlier. Output of the consumer electrical and electronic products and the textiles industries also dipped, by 14.8% and 11.3% respectively. Output of the plastic products, the wearing apparel, and the paper products and printing industries declined more moderately, by 7.3%, 5.0% and 3.3% respectively. On a seasonally adjusted quarter-to-quarter comparison, the Index fell by 6.5% in the second quarter of 2003, exacerbated from the 2.2% decrease in the first quarter.

Table 3.2

Index of Industrial Production for the major local manufacturing industries (year-on-year rate of change in volume (%))

	<u>2002</u>					<u>2003</u>	
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2[#]</u>
<u>Industry group</u>							
Wearing apparel	-6.6	-13.4	-10.5	4.0	-7.2	-0.1	-5.0
Textiles	-7.2	-10.6	-7.3	-5.9	-6.4	-0.8	-11.3
Plastic products	-10.8	-13.1	-7.4	-15.5	-7.0	-6.0	-7.3
Consumer electrical and electronic products	-23.6	-0.8	-29.6	-28.2	-35.4	-30.0	-14.8
Machinery and equipment	-16.8	-17.4	-19.7	-11.4	-18.8	-25.4	-30.4
Fabricated metal products	-29.4	-27.4	-30.7	-30.6	-28.8	-27.5	-21.5
Paper products and printing	-0.2	-10.5	1.0	0.1	8.3	11.7	-3.3
Overall manufacturing	-9.8	-11.6	-11.2	-7.3	-9.2	-8.8	-12.5
		<-2.4>	<-1.3>	<-0.7>	<-3.9>	<-2.2>	<-6.5>

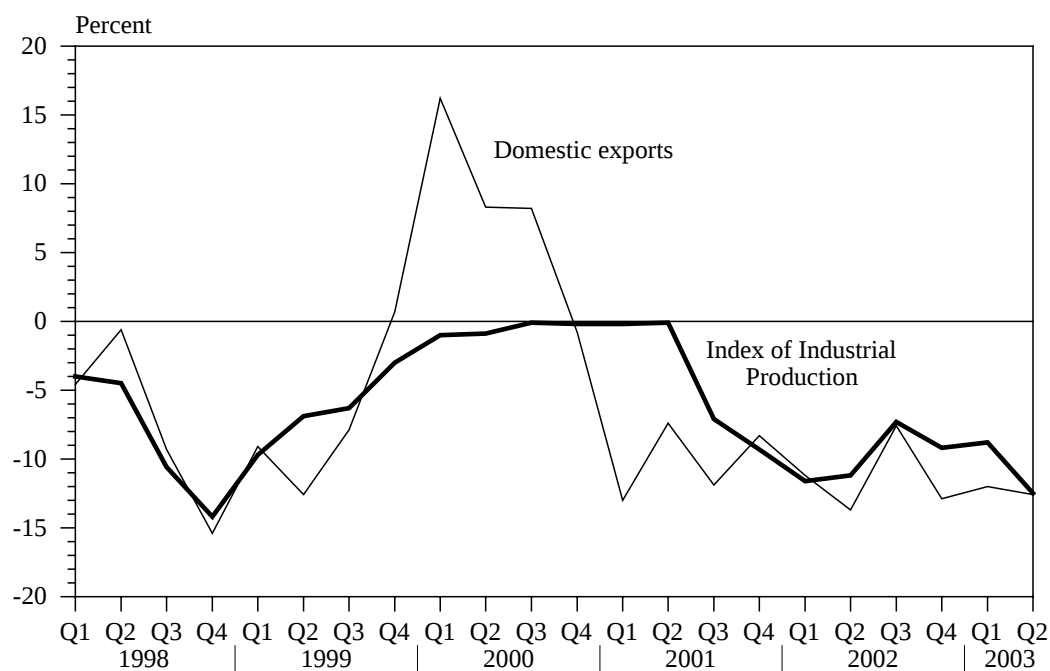
Notes : (#) Provisional figures.

< > Seasonally adjusted quarter-to-quarter % change in volume.

/Diagram 3.1

Diagram 3.1

**Local manufacturing output and domestic exports
(year-on-year rate of change in real terms)**



3.4 In the third quarter of 2003, domestic exports went down further from a year earlier, as did orders-on-hand in the local manufacturing sector⁽⁴⁾. These pointed to a further shrinkage in local manufacturing output in that quarter.

/Diagram 3.2

Diagram 3.2

**Orders-on-hand and domestic exports
(year-on-year rate of change in value terms)**

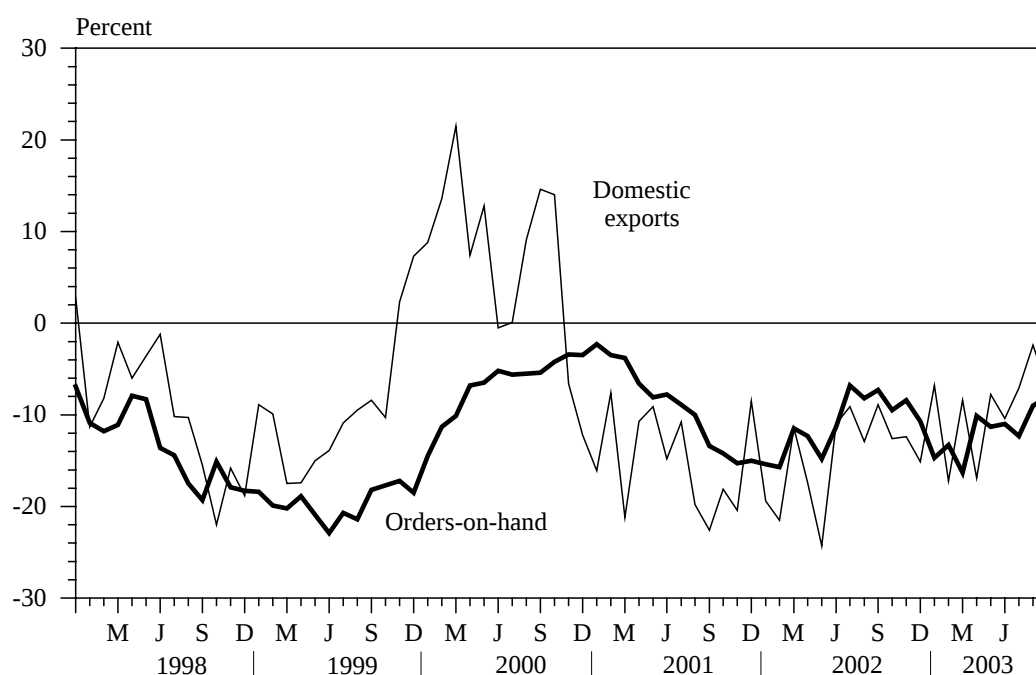


Table 3.3

Orders-on-hand in the local manufacturing sector

		<u>Value index of orders-on-hand (1993=100)</u>	<u>Year-on-year rate of change in value terms (%)</u>
2002	Mar	54.1	-11.5
	Jun	55.6	-11.3
	Sep	49.2	-7.3
	Dec	42.4	-10.7
2003	Mar	45.3	-16.3
	Jun	49.5	-11.0
	Sep [#]	45.2	-8.1

Note : (#) Provisional figures.

/Service

Service sector receipts

3.5 Business receipts in most of the service sectors surveyed declined in the second quarter of 2003. In some of the service sectors, the decline was rather more pronounced. Analysed by constituent sector and in value terms, business receipts in hotels and restaurants plummeted the most, by 64.3% and 19.2% respectively in the second quarter of 2003 over a year earlier, owing to the abrupt setback in inbound tourism and local consumption upon the impact of SARS in that quarter. Business receipts in the wholesale trade and the retail trade were likewise hit by SARS, dipping by 13.7% and 11.0% respectively. Business receipts in real estate, with reduced transactions in the property market, slid by 12.1%. Business receipts in transport fell by 10.9%, mainly on account of the suspension of schooling during the SARS period. Business receipts in storage decreased by 8.3%, amidst lower rental charges for storage space. Business receipts in film entertainment, financing (except banking), communications and business services also fell, by 5.6%, 5.5%, 4.9% and 3.7% respectively.

3.6 On the other hand, business receipts in insurance surged by 14.4% in the second quarter of 2003 over a year earlier, mainly upon further expansion in the life insurance segment. Business receipts in the import/export trade and banking rose moderately, by 4.3% and 2.3% respectively.

/Table 3.4

Table 3.4

**Index of Business Receipts for individual service sectors
(year-on-year rate of change in value terms (%))**

		<u>2002</u>				<u>2003</u>	
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
<u>Service sector</u>							
Import/export trade	-2.8	-15.4	-2.6	1.8	5.3	2.4	4.3
Wholesale trade	-10.7	-14.7	-12.8	-8.9	-6.2	-3.5	-13.7
Retail trade	-4.1	-3.7	-5.8	-4.3	-2.4	-2.6	-11.0
Restaurants	-5.4	-5.4	-6.0	-4.5	-5.9	-8.6	-19.2
Hotels	-2.3	-12.5	-6.6	-2.5	12.5	-2.7	-64.3
Banking	-0.8	-7.2	0.3	-4.2	7.4	-1.3	2.3
Financing (except banking)	-14.3	-25.2	-11.4	-6.9	-11.1	-5.7	-5.5
Insurance	10.3	10.0	6.0	9.8	15.0	22.4	14.4
Real estate	-2.5	-0.1	3.5	-8.4	-5.2	-4.3	-12.1
Business services	-5.8	-10.4	-4.0	-5.0	-3.5	0.2	-3.7
Transport	2.3	-8.2	0.3	6.1	10.6	5.6	-10.9
Storage	-19.6	-21.7	-27.4	-20.4	-6.8	-7.8	-8.3
Communications	-2.6	-5.2	-4.3	-1.4	0.5	1.6	-4.9
Film entertainment	-9.1	2.6	-15.5	-18.9	-1.8	-1.0	-5.6

/Property

Property

3.7 Activity in the sales market for *residential property* showed a strong pick-up during the third quarter of 2003. Sentiment improved markedly, along with the better performance of the overall economy and the strong rally in the stock market. This was particularly so after the signing of CEPA in June and implementation of the “individual visit” scheme for Mainland visitors to Hong Kong in July. Expectation for further policy measures to stabilise the housing market also provided some support⁽⁵⁾. Developers resumed sales in the primary market, which had been held off during the spread of SARS, and the sales were generally met with a good response. In view of this favourable turn, many developers had reduced or withdrawn the price discounts and other concessions they offered earlier⁽⁶⁾. Moreover, there was a notable revival in activity in the secondary market. Flat prices appeared to have bottomed out in the third quarter, with a slight increase recorded in September. In the luxury end of the market, the rebound was more clearly visible. Purportedly, the Government’s new policy measure to attract investment immigrants to Hong Kong rendered some lift to this segment⁽⁷⁾. As to the rental market, leasing activity likewise increased in the third quarter. Flat rentals also appeared to have stabilised towards the end of the quarter.

3.8 On a quarter-to-quarter comparison, the fall in flat prices narrowed, on average to 2% in the third quarter of 2003, from that of 5% in the second quarter. The fall in flat rentals likewise narrowed, on average to 2% in the third quarter of 2003, from that of 4% in the second quarter. For the first three quarters of 2003 as a whole, flat prices on average went down by 10%, and flat rentals by 9%. Compared with the respective peak levels in the third quarter of 1997, flat prices and rentals in the third quarter of 2003 remained substantially lower, by an average of 66% and 49% respectively.

/Box 3.1

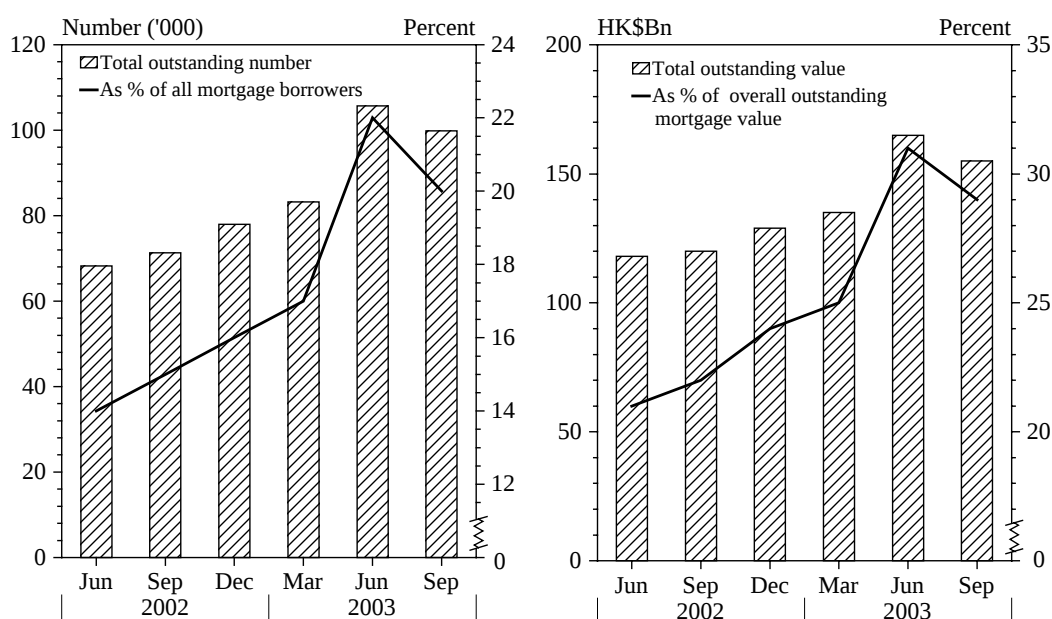
Box 3.1

Residential mortgage loans in negative equity

The dip in flat prices since late 1997 has impinged on people's wealth and hence on their consumption. This has been one of the underlying factors leading to the weak domestic demand in Hong Kong in recent years. Of particular concern is the large number of negative equity home owners, where the value of the residential property has fallen below the corresponding outstanding amount of mortgage loan. The quarterly survey on residential mortgage loans in negative equity conducted by the Hong Kong Monetary Authority, though covers primarily first mortgages, provides some useful indication about the situation.

According to the results of the latest survey, the total number of residential mortgage loans in negative equity amounted to 99 805 at end-September 2003, representing 20% of all residential mortgage borrowers. The corresponding aggregate value of mortgage loans in negative equity was around \$155 billion, representing 29% of the total amount of outstanding residential mortgage loans. These improved somewhat from the situation at end-June 2003, thanks to the recent pick-up in the residential property market. Actually, many of the new negative equity cases in the recent quarters were only marginally in negative equity.

Number and total amount of residential mortgage loans in negative equity



Despite the still large number of residential mortgage loans in negative equity, the banks' delinquency ratio for all outstanding residential mortgage loans, which measures the proportion of the total amount of loans overdue for three months to the overall outstanding amount of such loans, was at a low level of 1.05% at end-September 2003, improved from 1.12% at end-June.

3.9 On *commercial property*, both the sales and rental markets for *office space* turned more active in the third quarter of 2003. Investor interest was rekindled somewhat, stimulated in part by the signing of CEPA in June. Leasing demand also strengthened slightly. In addition, more tenants were willing to relocate their offices from buildings which were older or in secondary locations to better ones, as rentals of Grade A office space had fallen to a more attractive level to them. Yet the abundant supply of new and existing office space in overall terms continued to exert a drag on prices and rentals. On a quarter-to-quarter comparison, prices for office space on average remained virtually unchanged in the third quarter of 2003, after a 5% fall in the second quarter. For the first three quarters of 2003 as a whole, there was on average a 9% decrease. Office rentals declined appreciably further, on average by 6% in the third quarter of 2003, following a 5% fall in the second quarter. For the first three quarters of 2003 as a whole, the decrease on average amounted to 15%. Against their respective peak levels in 1994, prices and rentals for office space in the third quarter of 2003 plunged by an average of 75% and 63% respectively.

3.10 The sales and rental markets for *shopping space* both showed a mixed performance in the third quarter of 2003. Retail premises in popular locations and in better-managed shopping malls fared better, supported by the recovery in local consumer demand and in inbound tourism from the earlier SARS impact. On a quarter-to-quarter comparison, rentals for shopping space on average fell by 1% in the third quarter of 2003, having fallen by 6% in the second quarter. For the first three quarters of 2003 as a whole, there was on average a 10% decline. Prices for shopping space on average increased by 1% in the third quarter of 2003, after a similar increase in the second quarter. For the first three quarters of 2003 as a whole, there was on average virtually no change. Compared with the peak levels in the third quarter of 1997, prices and rentals for shopping space in the third quarter of 2003 plummeted by an average of 57% and 33% respectively.

/3.11

3.11 On *industrial property*, the sales and rental markets remained generally sluggish in the third quarter of 2003. Nevertheless, projects involving the conversion of industrial sites to hotel use gained some momentum, amidst the rebound in inbound tourism. On a quarter-to-quarter comparison, prices for industrial space on average came down by 2% in the third quarter of 2003, after a 4% decline in the second quarter. For the first three quarters of 2003 as a whole, prices for industrial space on average dropped by 6%. Rentals for industrial space on average were lower by 4% in the third quarter of 2003, following a 7% decline in the second quarter. For the first three quarters of 2003 as a whole, rentals for industrial space on average dipped by 12%. Against their respective peak levels in 1994, prices and rentals for industrial space in the third quarter of 2003 slumped by an average of 70% and 53% respectively.

3.12 Overall property transactions, as measured by agreements for sale and purchase of property registered with the Land Registry, went up distinctly by 16% in number and to a lesser extent by 4% in total value in the third quarter of 2003 over a year earlier, reversing the respective declines of 31% and 40% in the second quarter. Within these, transactions in residential property increased by 16% in number and 11% in total value in the third quarter of 2003 over a year earlier, as against the respective declines of 35% and 44% in the second quarter. Transactions in non-residential property increased by 15% in number but decreased by 17% in total value, in the third quarter of 2003 over a year earlier, as compared to the respective declines of 5% and 19% in the second quarter. For the first nine months of 2003 as a whole, overall property transactions still went down, by 14% in number and 22% in total value over a year earlier. Within these, transactions in residential property fell by 17% in number and 24% in total value, while transactions in non-residential property increased by 1% in number but decreased by 10% in total value. On a quarter-to-quarter comparison, overall property transactions increased markedly in the third quarter of 2003, by 29% in number and 36% in total value, in sharp contrast to the respective declines of 1% and 9% in the second quarter. Within these, transactions in residential property bounced up by 31% in number and 33% in total value in the third quarter of 2003, after a zero change in number and a 10% decline in total value in the second quarter. Transactions in non-residential property leaped by 19% in number and 47% in total value in the third quarter of 2003, following the respective declines of 5% and 3% in the second quarter.

/3.13

3.13 Property transfer assignments, being a lagging indicator of property transactions, went down by 21% in number but went up slightly by 2% in total value in the third quarter of 2003 over a year earlier, after declines of 21% and 19% respectively in the second quarter. For the first nine months of 2003 as a whole, there were declines of 17% in number and 8% in total value over a year earlier. On a quarter-to-quarter comparison, property transfer assignments went up by 4% in number and 18% in total value in the third quarter of 2003, following decreases of 17% and 6% respectively in the second quarter. As to mortgage arrangements in the third quarter of 2003, there was a decrease of 28% in number over a year earlier, after a 26% decline in the second quarter. For the first nine months of 2003 as a whole, there was a decrease of 25% in number over a year earlier. On a quarter-to-quarter comparison, the number of mortgage arrangements shrank further by 3% in the third quarter of 2003, having fallen by 16% in the second quarter.

3.14 On Government-subsidised flats, there were no new sales of flats under the Home Ownership Scheme (HOS) and the Tenants Purchase Scheme (TPS) in the first three quarters of 2003, following the announcement in November 2002 to cease the production and sale of HOS flats and also to halt the sale of public rental flats under TPS.

/Table 3.5

Table 3.5**Indices of Property Prices and Rentals**

		<u>Residential flats</u>				<u>Office space</u>				<u>Shopping space</u>				<u>Conventional flatted factory space</u>			
		<u>Price index^(a)</u>		<u>Rental index^(b)</u>		<u>Price index</u>		<u>Rental index^(b)</u>		<u>Price index</u>		<u>Rental index^(b)</u>		<u>Price index</u>		<u>Rental index^(b)</u>	
		(1999=100)		(1999=100)		(1999=100)		(1999 =100)		(1999=100)		(1999=100)		(1999=100)		(1999=100)	
2002	Q1	73.8	(*)	87.4	(-4)	71.2	(*)	89.6	(-6)	84.4	(*)	94.0	(-3)	75.4	(-3)	85.5	(-2)
	Q2	72.2	(-2)	84.8	(-3)	68.8	(-3)	85.4	(-5)	86.6	(3)	92.6	(-1)	76.9	(2)	83.0	(-3)
	Q3	68.6	(-5)	82.4	(-3)	68.6	(*)	84.0	(-2)	86.1	(-1)	92.8	(*)	74.4	(-3)	81.1	(-2)
	Q4	65.1	(-5)	79.0	(-4)	64.9	(-5)	82.7	(-2)	83.0	(-4)	92.1	(-1)	72.6	(-2)	81.2	(*)
2003	Q1	62.7	(-4)	76.6	(-3)	62.1	(-4)	79.4	(-4)	81.0	(-2)	89.1	(-3)	72.5	(*)	79.4	(-2)
	Q2 [^]	59.5	(-5)	73.3	(-4)	58.7	(-5)	75.1	(-5)	82.0	(1)	83.9	(-6)	69.9	(-4)	74.0	(-7)
	Q3 [^]	58.4	(-2)	71.5	(-2)	58.9	(*)	70.4	(-6)	82.7	(1)	83.2	(-1)	68.3	(-2)	71.1	(-4)

Notes : All rental indices shown in this table have been adjusted for changes in concessionary leasing terms such as provision of refurbishment, granting of rent-free periods, and waiver of miscellaneous charges, if known.

(a) Prices for residential property in this table cover existing flats traded in the secondary market, but not new flats sold in the primary market.

(b) Rentals for residential property in this table cover only new tenancies for which rentals are freshly determined, while rentals for non-residential property in this table cover also lease renewals upon which rentals may be revised.

() % change over the preceding quarter.

([^]) Provisional figures.

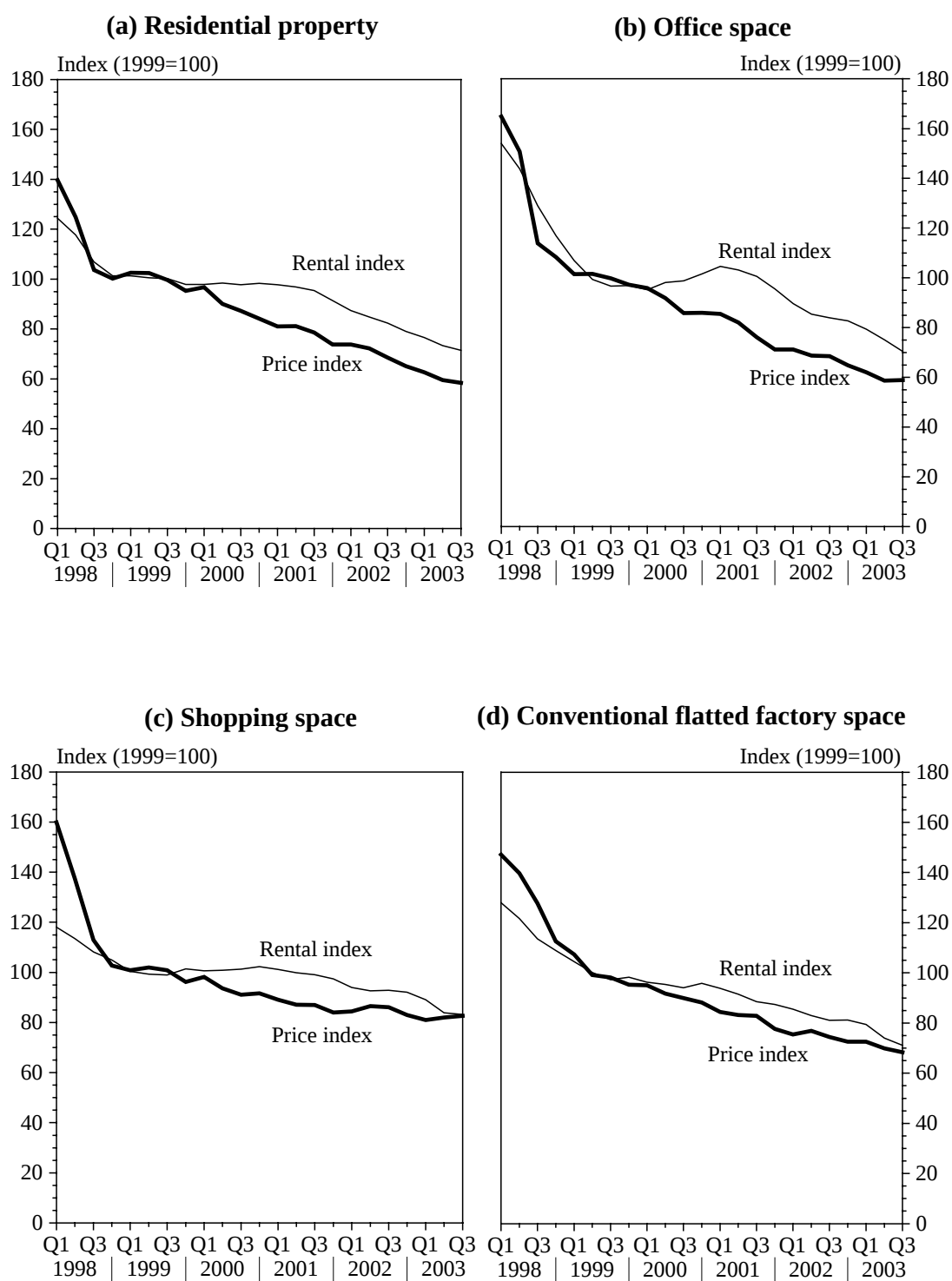
(*) Change of less than 0.5%.

Source : Rating and Valuation Department.

/Diagram 3.3

Diagram 3.3

Property prices and rentals



Note : See the footnotes to Table 3.5.

/Table 3.6

Table 3.6

**Relationship between mortgage rate
and monthly instalment payment**

		Average of the best lending rates quoted by the principal banks <u>in Hong Kong</u> (%)	Average of the effective mortgage rates charged on new mortgages by the principal banks <u>in Hong Kong</u> ^(a) (%)	Monthly instalment on \$100,000 mortgage loan charged according to the average effective mortgage rate with mortgage period of ^(b) (<u>\$</u>)		
				<u>10 years</u>	<u>15 years</u>	<u>20 years</u>
2002	Q1	5.13	2.63	949	673	536
	Q2	5.13	2.63	949	673	536
	Q3	5.13	2.63	949	673	536
	Q4	5.07	2.55	945	669	533
2003	Q1	5.00	2.50	943	667	530
	Q2	5.00	2.50	943	667	530
	Jan	5.00	2.50	943	667	530
	Feb	5.00	2.50	943	667	530
	Mar	5.00	2.50	943	667	530
	Apr	5.00	2.50	943	667	530
	May	5.00	2.50	943	667	530
	Jun	5.00	2.50	943	667	530
	Jul	5.00	2.50	943	667	530
	Aug	5.00	2.50	943	667	530
	Sep	5.00	2.50	943	667	530

Notes : (a) Here the effective mortgage rate refers to the modal value, representing the rate most commonly charged to customers amongst the banks.

(b) These figures are based on equal monthly repayments throughout the mortgage period.

3.15 As a common indicator of the supply of new property, *completions* of private residential flats decreased by 26% in the third quarter of 2003 over a year earlier, after a mild increase of 4% in the second quarter. Completions of office space surged substantially further from a low base, by 224% in the third quarter, following a 199% leap in the second quarter. Completions of other commercial premises dropped by 69% in the third quarter, having risen by 23% in the second quarter. As to industrial property, there were no completions in

/both

both the second and third quarters. Comparing the first nine months of 2003 with a year earlier, completions of office space, industrial property and other commercial premises all went up, by 93%, 474% and 9% respectively, while completions of private residential flats went down by 7%.

Table 3.7

Agreements for sale and purchase of property

		<u>Number</u>						<u>Total value (\$Bn)</u>					
		<u>Residential property^(a)</u>		<u>Non-residential Property</u>		<u>Total</u>		<u>Residential property^(a)</u>		<u>Non-residential Property</u>		<u>Total</u>	
2002	Annual	72 974	(5)	12 947	(-30)	85 921	(-3)	154.3	(2)	31.1	(-26)	185.4	(-4)
	H1	40 921	(25)	6 877	(-37)	47 798	(9)	89.9	(27)	14.4	(-38)	104.3	(11)
	H2	32 053	(-13)	6 070	(-19)	38 123	(-14)	64.4	(-19)	16.7	(-11)	81.1	(-18)
	Q1	18 992	(26)	3 569	(-40)	22 561	(7)	41.5	(21)	6.1	(-44)	47.7	(5)
	Q2	21 929	(24)	3 308	(-35)	25 237	(11)	48.3	(32)	8.3	(-32)	56.6	(16)
	Q3	16 120	(-11)	3 277	(-12)	19 397	(-11)	32.3	(-22)	11.9	(37)	44.2	(-11)
	Q4	15 933	(-15)	2 793	(-26)	18 726	(-17)	32.1	(-17)	4.8	(-52)	36.9	(-24)
2003	H1	28 722	(-30)	6 478	(-6)	35 200	(-26)	56.9	(-37)	13.7	(-5)	70.6	(-32)
	Q1-Q3	47 438	(-17)	10 233	(1)	57 671	(-14)	92.8	(-24)	23.7	(-10)	116.5	(-22)
	Q1	14 386	(-24)	3 329	(-7)	17 715	(-21)	29.9	(-28)	7.0	(14)	36.9	(-23)
	Q2	14 336	(-35)	3 149	(-5)	17 485	(-31)	27.0	(-44)	6.8	(-19)	33.7	(-40)
	Q3	18 716	(16)	3 755	(15)	22 471	(16)	35.9	(11)	9.9	(-17)	45.9	(4)
		<31>		<19>		<29>		<33>		<47>		<36>	
	Jan	6 187	(-21)	1 106	(-20)	7 293	(-21)	12.0	(-34)	2.6	(5)	14.6	(-29)
	Feb	3 649	(-36)	973	(-14)	4 622	(-32)	6.4	(-48)	1.6	(-4)	8.0	(-43)
	Mar	4 550	(-17)	1 250	(19)	5 800	(-11)	11.5	(5)	2.8	(40)	14.3	(10)
	Apr	5 373	(-27)	1 009	(-4)	6 382	(-25)	10.5	(-31)	2.3	(16)	12.8	(-26)
	May	4 130	(-44)	960	(-16)	5 090	(-40)	7.5	(-56)	1.9	(-44)	9.4	(-54)
	Jun	4 833	(-33)	1 180	(6)	6 013	(-28)	9.0	(-44)	2.5	(-13)	11.5	(-40)
	Jul	6 525	(32)	1 133	(-6)	7 658	(24)	12.5	(22)	4.2	(-23)	16.7	(6)
	Aug	6 559	(34)	1 388	(18)	7 947	(31)	12.2	(24)	3.1	(-13)	15.3	(14)
	Sep	5 632	(-10)	1 234	(37)	6 866	(-4)	11.2	(-7)	2.6	(-9)	13.9	(-7)

Notes : Figures may not add up exactly to the total due to rounding.

- (a) It should be noted that primary sales of units under the Home Ownership Scheme (HOS) and the Tenants Purchase Scheme (TPS) are not covered in this table, as sale and purchase agreements are commonly not required for these transactions. Also, sale and purchase agreements for primary sales of units under the Private Sector Participation Scheme (PSPS) are not included in the column on residential property, yet they are included in the column on non-residential property, and thus also in the total column.

() % change over a year earlier.

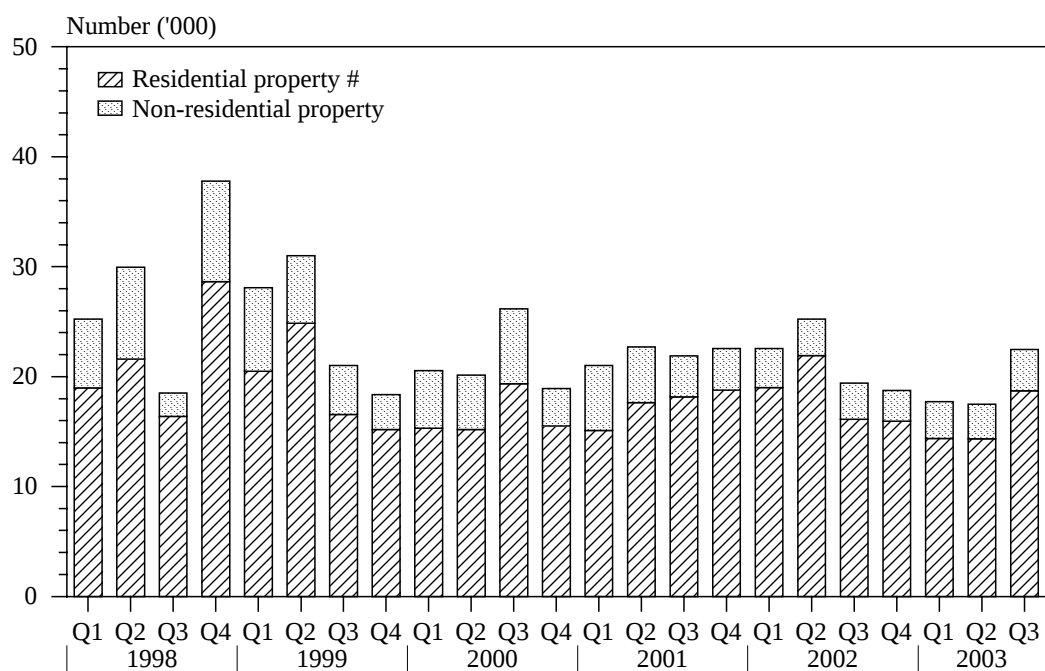
< > % change over the preceding quarter.

Source : Land Registry.

/Diagram 3.4

Diagram 3.4

Sale and purchase agreements by broad type of property



Note : (#) See Footnote (a) to Table 3.7.

/Table 3.8

Table 3.8**Property transfer assignments and mortgage arrangements**

		<u>Property transfer assignments</u> ^(a)				<u>Mortgages other than building mortgages</u> ^(b)	
		<u>Number</u>		<u>Total value (\$Bn)</u>		<u>Number</u>	
2002	Annual	119 734	(-17)	198.1	(-19)	121 791	(-22)
	H1	61 350	(-19)	100.5	(-20)	64 384	(-19)
	H2	58 384	(-14)	97.6	(-17)	57 407	(-26)
	Q1	31 512	(-19)	48.5	(-24)	33 650	(-18)
	Q2	29 838	(-19)	52.0	(-17)	30 734	(-21)
	Q3	30 998	(-24)	49.1	(-36)	30 721	(-33)
	Q4	27 386	(*)	48.5	(18)	26 686	(-14)
2003	H1	52 175	(-15)	87.3	(-13)	49 698	(-23)
	Q1-Q3	76 813	(-17)	137.2	(-8)	71 778	(-25)
	Q1	28 557	(-9)	45.0	(-7)	26 941	(-20)
	Q2	23 618	(-21)	42.3	(-19)	22 757	(-26)
	Q3	24 638	(-21)	49.9	(2)	22 080	(-28)
			<4>		<18>		<-3>
	Jan	10 895	(-10)	16.2	(-25)	10 294	(-23)
	Feb	9 283	(11)	16.2	(29)	9 097	(-2)
	Mar	8 379	(-25)	12.6	(-12)	7 550	(-32)
	Apr	8 748	(-5)	16.1	(-5)	8 288	(-11)
	May	8 597	(-4)	14.9	(7)	8 481	(-6)
	Jun	6 273	(-47)	11.2	(-47)	5 988	(-52)
	Jul	7 343	(-42)	17.9	(-19)	6 125	(-54)
	Aug	7 404	(-29)	16.0	(5)	6 124	(-38)
	Sep	9 891	(24)	16.0	(36)	9 831	(29)

Notes : (a) Figures on property transfer assignments do not necessarily tally with those on agreements for sale and purchase of property, for various reasons. These include possibly long time lag between the two documents, cancellation of transaction before its completion, and waiver of the agreement for sale and purchase of property subject to consent by the parties concerned.

(b) Most of these mortgages are related to the purchase of residential flats or of other premises. Building mortgages, on the other hand, are related to the financing of building projects under construction.

Figures on the total value of mortgage arrangements are not shown, as they are likely to be incomplete. This is because in many of the mortgage arrangements lodged for registration, the value of the mortgage loan is not stated in the mortgage deed but instead is separately notified by the bank to the mortgagor.

() % change over a year earlier.

< > % change over the preceding quarter.

(*) Change of less than 0.5%.

Source : Land Registry.

/Table 3.9

Table 3.9

**Completions of new property by the private sector
(’000m² of internal floor area)**

<u>Usage</u>	<u>Third quarter of 2002</u>	<u>Third quarter of 2003[^]</u>	<u>Year- on-year rate of change (%)</u>	<u>Jan-Sep of 2002</u>	<u>Jan-Sep of 2003[^]</u>	<u>Year- on-year rate of change (%)</u>
Residential ^(a)	13 348	9 816	-26	22 976	21 375	-7
Commercial	49	41	-17	194	306	58
<i>Of which:</i>						
Office space	9	28	224	114	219	93
Other commercial premises (mainly shopping space) ^(b)	41	13	-69	80	87	9
Industrial ^(c)	0	0	--	3	16	474
<i>Of which:</i>						
Industrial-cum-office premises	0	0	--	0	16	--
Flatted factory space	0	0	--	3	0	-100
Storage premises ^(d)	0	0	--	0	0	--

Notes : (a) These include all newly completed residential premises to which either temporary or full Occupation Permits have been granted, as well as village-type houses issued with Letters of Compliance. Property developments subject to a Consent Scheme will need a Certificate of Compliance, Consent to Assign or Consent to Lease in addition to an Occupation Permit before the premises can be individually assigned.

The figures shown are in respect of private residential units, excluding units completed by the Hong Kong Housing Authority and Hong Kong Housing Society.

(b) These include shopping arcades in residential and commercial developments, as well as premises designed or adapted for commercial use other than offices, in the nature of non-domestic space on the podium floors of tenement apartment/commercial buildings. Car-parking space is excluded.

(c) Including industrial-cum-office premises but excluding specialised factory buildings, which are developed mainly for own use.

(d) Including storage premises at the container terminals and the airport.

([^]) Provisional figures.

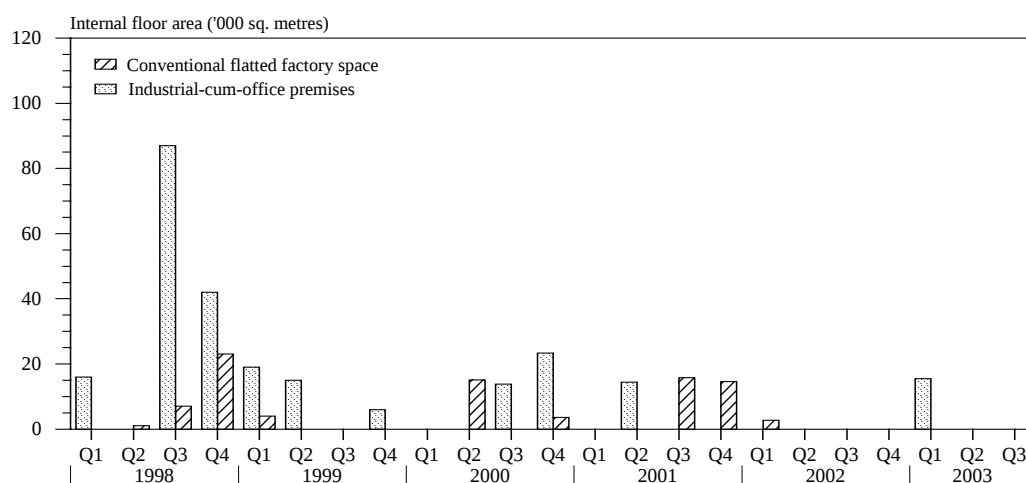
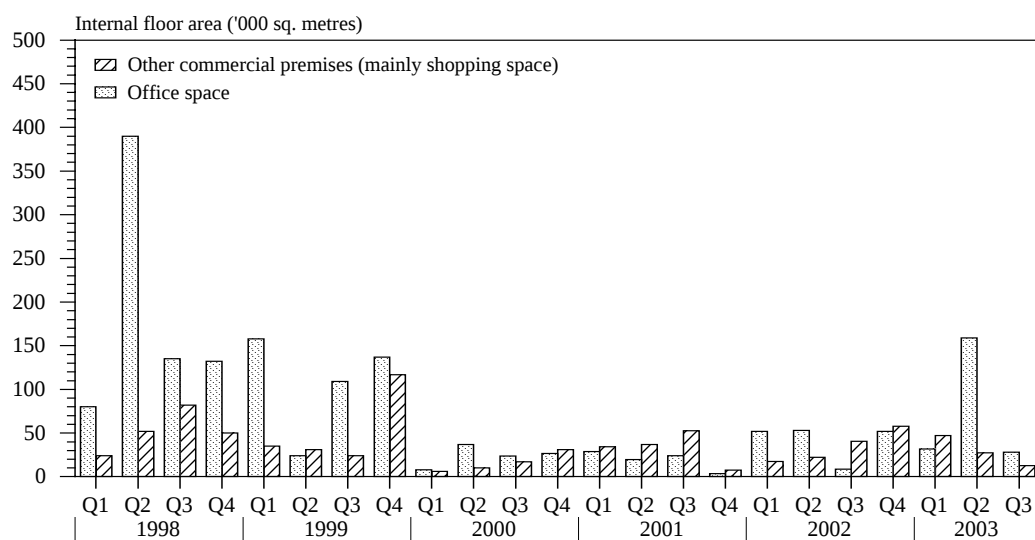
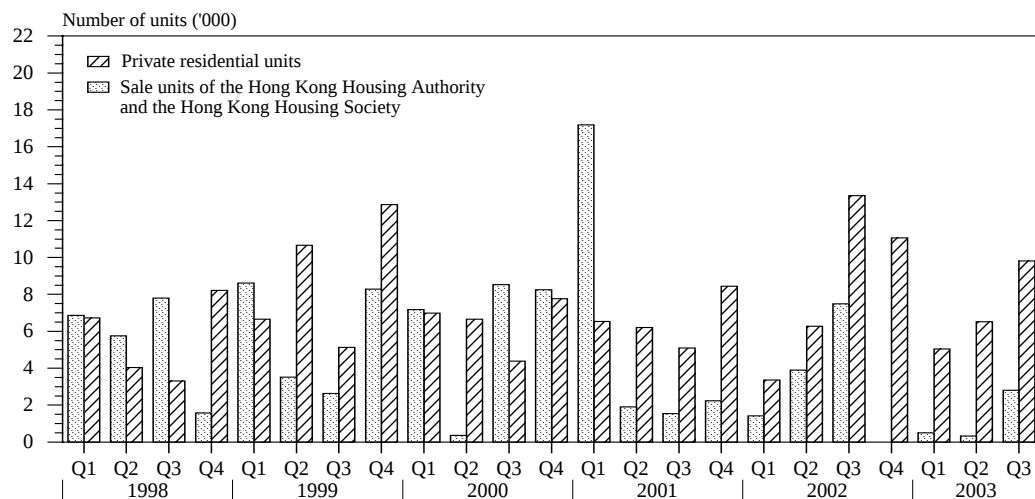
(--) Not applicable.

Source : Rating and Valuation Department.

/Diagram 3.5

Diagram 3.5

Completions of new property by major category



Note : See the footnotes to Table 3.9.

3.16 *Planned developments* of all types of property in the private sector, as indicated by the total usable floor area on building plans with consent to commence work, went up by 22% in the third quarter of 2003 over a year earlier, after an 18% decrease in the second quarter. Analysed by main type of property and on a year-on-year comparison, planned developments of private residential property increased by 38% in terms of units or by 1% in terms of total usable floor area in the third quarter of 2003, in contrast to the corresponding decreases of 11% and 39% in the second quarter. On the other hand, planned developments of commercial property plummeted further from a high base, by 48% in the third quarter, after a 59% plunge in the second quarter. Planned developments of industrial property in both the second and third quarters were negligible in terms of total usable floor area. Planned developments of property in the “others” category continued to surge from a low base, by 300% in the third quarter, following a 665% leap in the second quarter. Comparing the first nine months of 2003 with a year earlier, planned developments of all types of property increased by 26%. Planned developments of private residential property rose by 74% in terms of units or by 23% in terms of total usable floor area. While planned developments of property in the “others” category surged by 372%, planned developments of commercial property and industrial property were down by 55% and 100% respectively.

/Table 3.10

Table 3.10

**Building plans with consent to
commence work in the private sector
(^{'000}m² of usable floor area)**

<u>Usage</u>	<u>Third quarter of 2002</u>	<u>Third quarter of 2003</u>	<u>Year-on-year rate of change (%)</u>	<u>Jan-Sep of 2002</u>	<u>Jan-Sep of 2003</u>	<u>Year-on-year rate of change (%)</u>
Residential ^(a)	185 (4 150)	186 (5 745)	1 (38)	637 (13 600)	781 (23 716)	23 (74)
Commercial	136	71	-48	266	118	-55
Industrial ^(b)	#	#	-85	32	#	-100
Others	48	191	300	80	376	372
Total	368	448	22	1 015	1 276	26

Notes : Figures may not add up exactly to the total due to rounding.

Developers are required to re-apply for issue of consent to commence work on every major revision of their development projects. The figures reported here may include re-application cases and hence are subject to double-counting. In the third quarter of 2003, for building plans with consent to commence work in respect of private residential property, 39% in terms of units or 37% in terms of total usable floor area were re-application cases. For the first nine months of 2003 as a whole, the corresponding proportions were 50% and 46%.

(a) Here the classification of residential property includes developments under the Urban Improvement Scheme of the Hong Kong Housing Society, but excludes developments under the Home Ownership Scheme and the Private Sector Participation Scheme of the Hong Kong Housing Authority.

(b) Including multi-purpose industrial premises designed also for office use.

() Number of units.

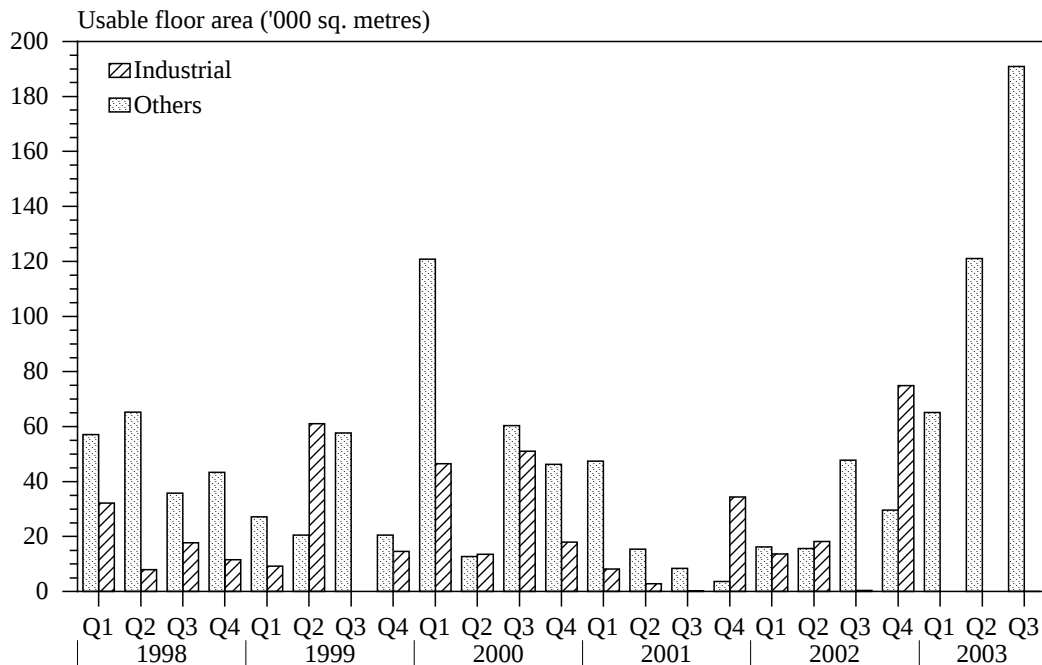
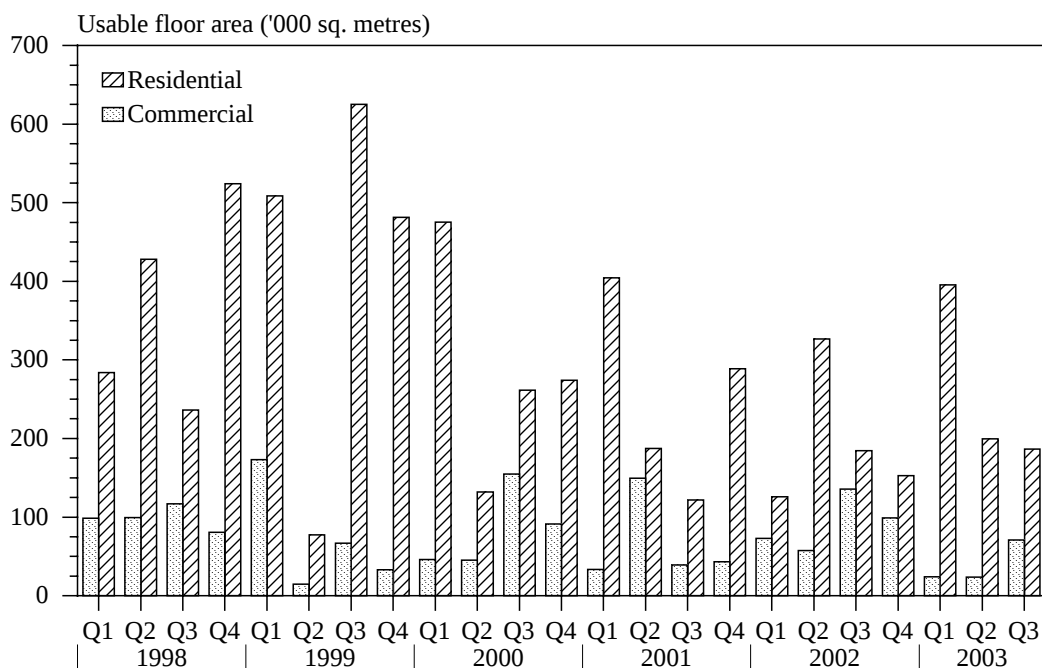
(#) Usable floor area of less than 500 m².

Source : Buildings Department.

/Diagram 3.6

Diagram 3.6

**Building plans with consent to commence work
in the private sector by major category**



Note : See the footnotes to Table 3.10.

Building and construction

3.17 Building and construction activity on the whole remained weak in the third quarter of 2003. Reflecting this, overall expenditure on building and construction contracted further, by 6% in real terms in the third quarter of 2003 over a year earlier, following an 8% fall in the second quarter. For the first three quarters of 2003 as a whole, there was a decrease of 6% over a year earlier, reversing the 1% increase in 2002.

3.18 Expenditure on building and construction by the public sector rebounded to a 13% rise in real terms in the third quarter of 2003, after a 1% drop in the second quarter. For the first three quarters of 2003 as a whole, there was a modest increase of 2% in real terms over a year earlier, reversing the 6% decline in 2002. Apart from the effect of a low base of comparison a year earlier, the rebound in the third quarter mainly reflected intensified civil engineering works on some major projects, including infrastructure in support of Container Terminal 9 and the Hong Kong Disneyland project in Penny's Bay, Route 9 and the Deep Bay Link, and the KCR Lok Ma Chau Spur Line. This offset the dampening effect from completion or winding down of civil engineering works on several KCR railway projects, including the West Rail, the Ma On Shan Extension and the Tsim Sha Tsui Extension, and from reduced building activity under the Public Housing Programme.

3.19 On the other hand, expenditure on building and construction by the private sector declined significantly further, by 13% in real terms in the third quarter of 2003 over a year earlier, having fallen by 11% in the second quarter. For the first three quarters of 2003 as a whole, there was a marked decline of 9% in real terms over a year earlier, in contrast to a 4% rise in 2002. Private sector building programmes, whilst slowing down in response to the earlier sluggishness in the property market, were also held back by postponement of the railway property developments and by suspension of land sales until the end of this year.

/Table 3.11

Table 3.11

**Expenditure on building and construction
(year-on-year rate of change in real terms (%))**

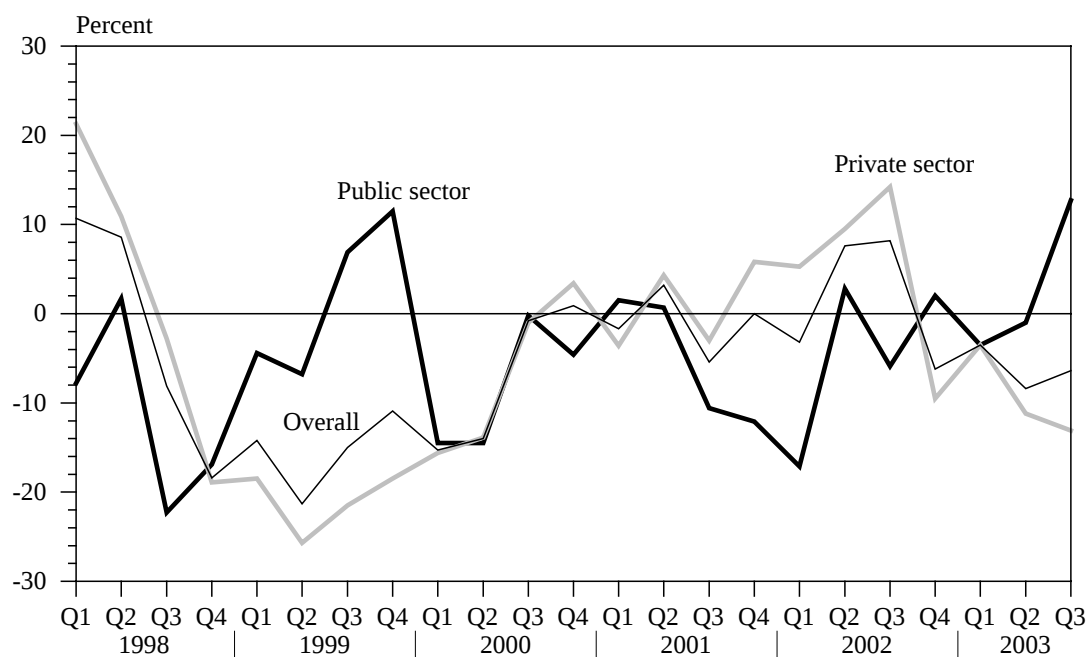
		<u>Private sector</u>	<u>Public sector</u>	<u>Total</u>
2002	Annual [#]	4	-6	1
	Q1 [#]	5	-17	-3
	Q2 [#]	10	3	8
	Q3 [#]	14	-6	8
	Q4 [#]	-10	2	-6
2003	H1 [#]	-8	-2	-6
	Q1-Q3 ⁺	-9	2	-6
	Q1 [#]	-4	-4	-4
	Q2 [#]	-11	-1	-8
	Q3 ⁺	-13	13	-6

Notes : (#) Revised figures.

(+) Preliminary figures.

Diagram 3.7

**Expenditure on building and construction
(year-on-year rate of change in real terms)**



/3.20

3.20 Retained imports of construction machinery went down distinctly further, by 29% in real terms in the third quarter of 2003 over a year earlier, after a 22% decline in the second quarter. For the first three quarters of 2003 as a whole, retained imports of construction machinery dipped by 21% in real terms over a year earlier, in contrast to an 11% increase in 2002. This was in line with the decline in overall building and construction activity in the same period.

3.21 Retained imports of general construction materials decreased by 17% in real terms in the third quarter of 2003 over a year earlier, after a 23% increase in the second quarter against a low base a year earlier. For the first three quarters of 2003 as a whole, retained imports of general construction materials increased by 12% over a year earlier, after a 10% decrease in 2002.

3.22 Labour cost in the building and construction sector, as measured by the Labour Cost Index, decreased by 2% in the second quarter of 2003 from a year earlier, having remained stable in the first quarter. Building material cost, as measured by the Material Cost Index, increased by 1% in the second quarter of 2003 from a year earlier, following a similar increase in the first quarter. Taken together, the combined Labour and Material Cost Index was 1% lower in the second quarter of 2003 as compared to a year earlier, having stayed flat in the first quarter. Compared with the preceding quarter, the Labour Cost Index decreased by 1% in the second quarter of 2003 while the Material Cost Index was virtually unchanged. This led to a 1% decrease in the combined Labour and Material Cost Index.

/Table 3.12

Table 3.12

**Labour and Material Cost Index for
the building and construction sector
(Feb 1970=100)**

		<u>Labour Index</u>		<u>Material Index</u>		<u>Combined Index</u>	
2002	Annual	3 575	(*)	754	(-1)	1 752	(*)
	Q1	3 570	(-1)	752	(-1)	1 749	(-1)
	Q2	3 588	(*)	753	(-1)	1 756	(*)
	Q3	3 583	(*)	755	(*)	1 755	(*)
	Q4	3 561	(*)	756	(*)	1 748	(*)
2003	Q1	3 574	(*)	759	(1)	1 754	(*)
	Q2	3 529	(-2)	759	(1)	1 739	(-1)
			<-1>		<*>		<-1>

Notes : () % change over a year earlier.

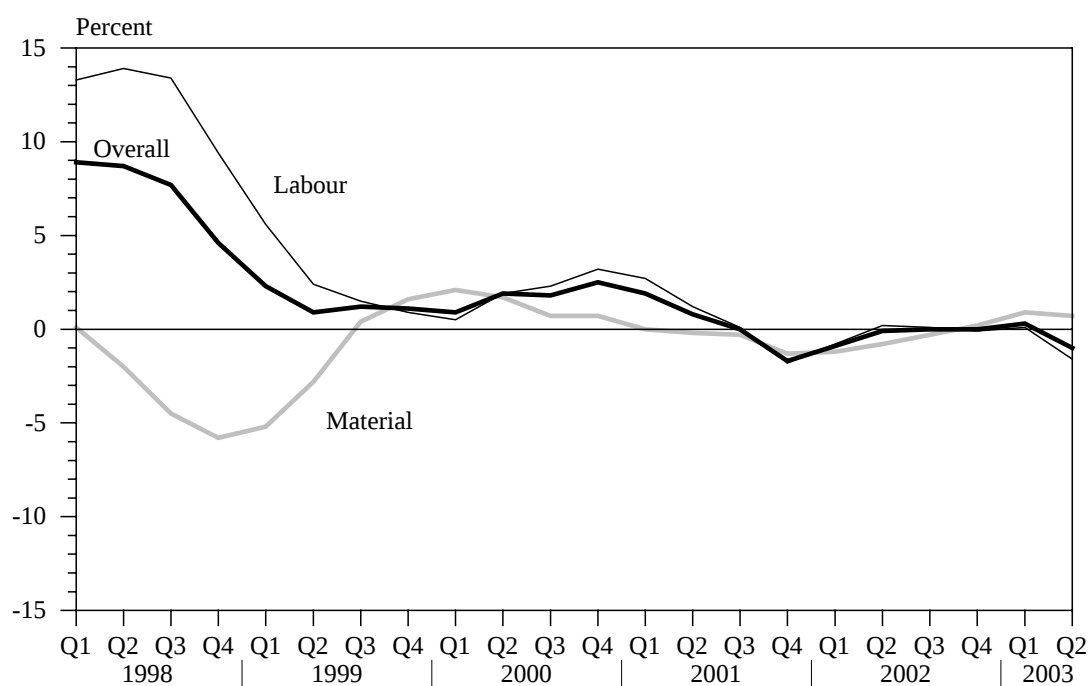
< > % change over the preceding quarter.

(*) Change of less than 0.5%.

Source : Architectural Services Department.

Diagram 3.8

**Labour and Material Cost Indices
(year-on-year rate of change)**



3.23 Tender prices remained soft. The Tender Price Index (TPI) for public housing projects compiled by the Housing Department went down further, by 11% in the second quarter of 2003 over a year earlier, after a 14% decline in the first quarter. This reflected continued keen competition for a much reduced volume of public housing projects. The TPI for public sector building projects compiled by the Architectural Services Department fell back by 3% in the second quarter of 2003 over a year earlier, after a 5% increase in the first quarter. Compared with the preceding quarter, both TPIs showed little change in the second quarter of 2003.

Table 3.13

Tender Price Indices (TPI) for public sector projects

		TPI for public <u>housing projects</u> ^(a) (Jan 1970=100)		TPI for public sector <u>building projects</u> ^(b) (Jan 1970=100)	
2002	Annual	527	(-10)	714	(-12)
	Q1	556	(-9)	687	(-20)
	Q2	533	(-13)	742	(-12)
	Q3	525	(-6)	692	(-14)
	Q4	495	(-10)	733	(2)
2003	Q1	476	(-14)	720	(5)
	Q2	474	(-11)	723	(-3)
		<*>		<*>	

Notes : (a) Compiled by the Housing Department.

(b) Compiled by the Architectural Services Department.

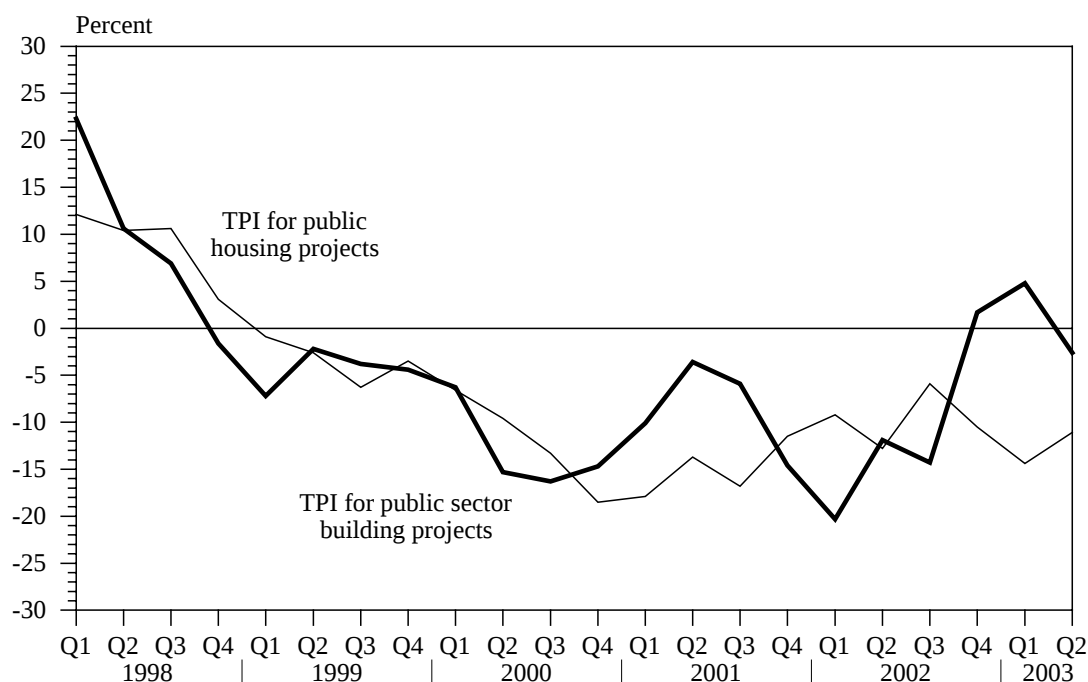
() % change over a year earlier.

< > % change over the preceding quarter.

/Diagram 3.9

Diagram 3.9

**Tender Price Indices
(year-on-year rate of change)**



Land

3.24 In the third quarter of 2003, there was no land sale at auction by the Government, following announcement in November 2002 of the decision to stop arranging scheduled land auctions and to suspend the Application List⁽⁸⁾ until December 2003, as part of the package of measures to stabilise the housing market. There was also no land sale through tender by the Government in the third quarter. For the first nine months of 2003 as a whole, only one commercial site of 1.2 hectares was sold through tender in May.

/Table 3.14

Table 3.14

**Land sales at auction and by tender
by the Government (hectares)**

<u>Usage</u>	<u>Jan-Sep of 2002</u>	<u>Jan-Sep of 2003</u>
Residential	6.4	-
Residential/commercial	0.1	-
Commercial	-	1.2
Industrial	-	-
Others	-	-
Total	<u>6.4</u>	<u>1.2</u>

Note : Figures may not add up exactly to the total due to rounding.

Source : Lands Department.

3.25 On modification of lease on existing developed and developable land in the private sector domain⁽⁹⁾, 24 applications were approved by the Government in the third quarter of 2003. Of this total, nine applications were for residential development, five for residential-cum-commercial development, one for commercial development, two for industrial development, one for education and community facilities, and the remaining six for other miscellaneous purposes. For the first nine months of 2003 as a whole, 76 applications for modification of lease were approved.

3.26 In the third quarter of 2003, there was no new take-up of sites in the three industrial estates at Tai Po, Yuen Long and Tseung Kwan O. Meanwhile, one site of 1.17 hectares in the Tai Po Industrial Estate was surrendered. As at end-September 2003, the take-up rates in these three industrial estates were 93.1%, 91.3% and 47.9% respectively.

3.27 As to the Science Park at Pak Shek Kok, approvals for admission were granted to four more technology companies in the third quarter of 2003. As at end-September 2003, 42 tenants were already admitted, including 14 incubatees⁽¹⁰⁾. Most of the companies admitted were engaged in the electronics, biotechnology, information technology and telecommunications,

/and

and precision engineering fields. The Science Park commenced operation in June 2002, upon completion of Phase 1a of the development project. The remainder of Phase 1 would be completed by mid-2004. Planning for Phase 2 was underway.

Electricity and gas

3.28 *Local electricity consumption* rose by 2% over a year earlier to 12 037 million kWh in the third quarter of 2003, reversing the 3% decrease in the second quarter. For the first nine months of 2003 as a whole, local electricity consumption remained virtually unchanged over a year earlier, following a 2% increase in 2002. Analysed by main user type, domestic consumption and commercial consumption both increased by 3% while industrial consumption decreased by 11% in the third quarter of 2003 over a year earlier. This compared with the respective decreases by 1%, 3% and 8% in the second quarter. Electricity exports to the Mainland, which accounted for 8% of the total electricity generated in Hong Kong, increased sharply, by 65% in the third quarter of 2003 over a year earlier, reversing the 12% decrease in the second quarter. For the first nine months of 2003 as a whole, electricity exports to the Mainland increased markedly, by 20% over a year earlier.

3.29 *Towngas consumption* in the third quarter of 2003 increased by 2% over a year earlier to 5 939 terajoules, following zero change in the second quarter. For the first nine months of 2003 as a whole, there was a 2% increase over a year earlier, having remained virtually unchanged in 2002. Analysed by main user type, domestic consumption and industrial consumption increased by 6% and 8% respectively in the third quarter of 2002 over a year earlier, more than offsetting the 4% decrease in commercial consumption. In the second quarter, the respective changes were 7%, -6% and -10%.

Internal transport

3.30 Total patronage on *public transport* declined by 2% over a year earlier to 1.0 billion in the third quarter of 2003. This was much narrowed from the 11% decline in the second quarter, mainly reflecting dilution of the SARS

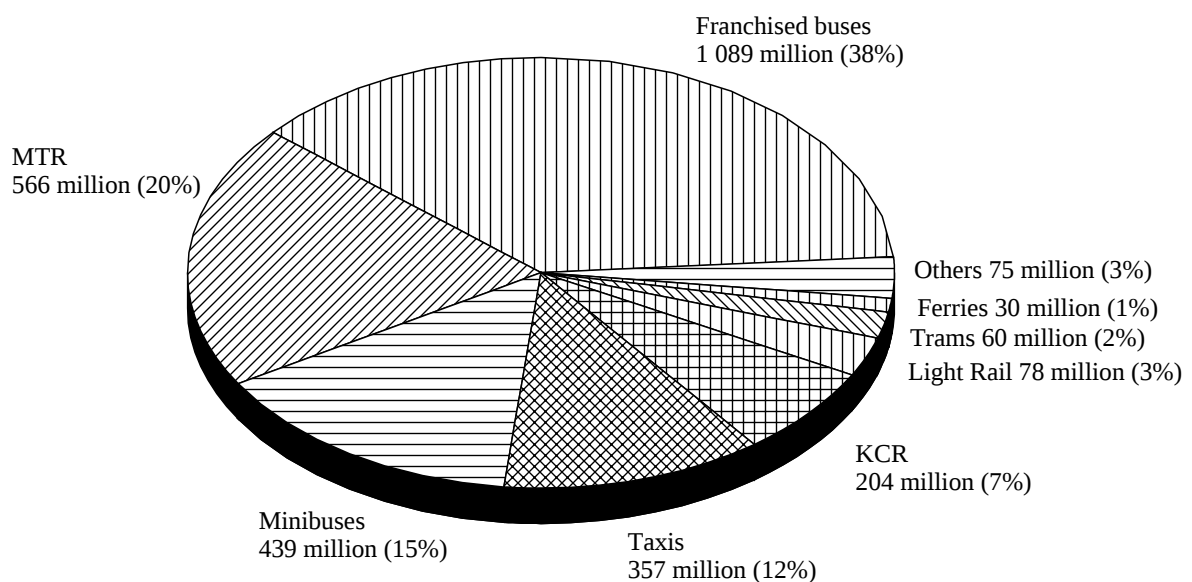
/impact.

impact. For the first nine months of 2003 as a whole, there was a 5% decline over a year earlier, in contrast to a 2% rise in 2002. Analysed by mode of transport, patronage on franchised buses and trams went down the most, by 5% and 4% respectively in the third quarter of 2003 over a year earlier, while patronage on the Light Rail, the Kowloon-Canton Railway and ferries fell by 3%, 3% and 2% respectively. On the other hand, patronage on mini-buses and the Mass Transit Railway rose by 2% and 1% respectively, while patronage on taxis remained steady.

3.31 On *private transport*, the total number of newly registered private cars declined markedly further, by 31% over a year earlier to 5 800 in the third quarter of 2003, following a 40% decline in the second quarter. For the first nine months of 2003 as a whole, there was a 28% decrease over a year earlier, widened from that of 13% in 2002. The total number of registered private cars, at 383 300 at end-September 2003, was similar to that a year earlier, while the total number of licensed private cars, at 338 200 at end-September 2003, decreased by 1% over a year earlier.

Diagram 3.10

**Passenger journeys by mode of public transport
in the first nine months of 2003**



Total passenger journeys in the first nine months of 2003 : 2 896 million

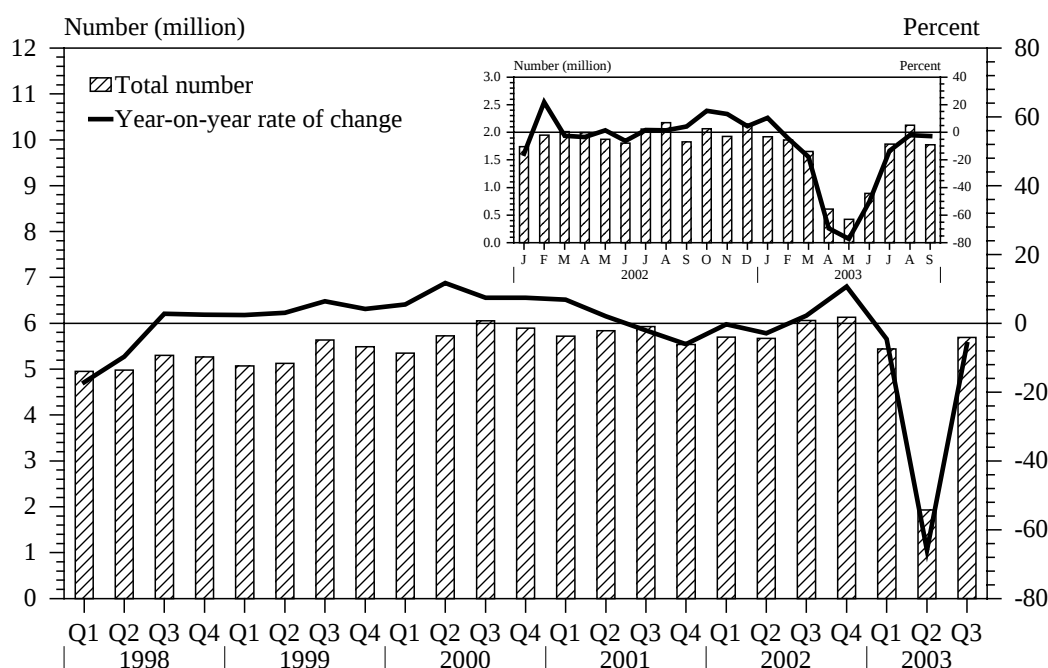
/External

External transport

3.32 On *air transport*, total *air passenger movements* declined moderately in the third quarter of 2003, by 6% over a year earlier to 5.7 million. Yet this compared more favourably with the 66% decline in the second quarter, when SARS exerted a severe impact on both inbound and outbound travel. Within the total for the third quarter, air passenger arrivals and departures decreased by 5% and 7% to 2.9 million and 2.8 million respectively. Air passengers coming from the Mainland still declined significantly by 12%, yet air passengers going to the Mainland rebounded visibly by 11%. For the first nine months of 2003 as a whole, total air passenger movements, air passenger arrivals and departures all fell markedly, by 25% from a year earlier. In 2002, there was an increase of 2%. Aircraft movements (including passenger and cargo flights) decreased by 10% over a year earlier to 48 000 in the third quarter of 2003, much narrowed from the 40% decrease in the second quarter. For the first nine months of 2003 as a whole, aircraft movements dropped by 14% over a year earlier, in contrast to the 5% rise in 2002.

Diagram 3.11

Number of air passenger movements

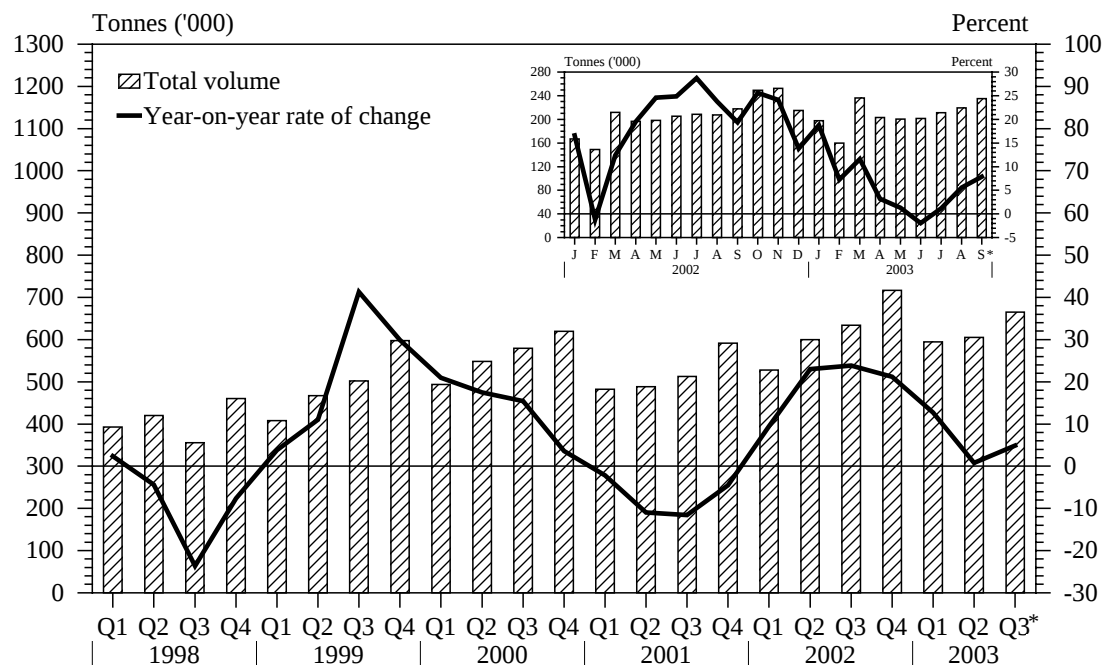


/3.33

3.33 Total *air cargo movements* went up moderately by 5% over a year earlier to 665 400 tonnes in the third quarter of 2003, faster than the 1% increase in the second quarter. Within the total for the third quarter, inward air cargo increased by 2% to 258 400 tonnes and outward air cargo increased by 7% to 407 000 tonnes, both underpinned by the continued growth in external trade. For the first nine months of 2003 as a whole, total air cargo movements rose by 6% over a year earlier, comprising increases of 2% and 8% respectively for inward and outward cargo. Yet these were much slower than the corresponding increases of 19%, 12% and 25% in 2002.

Diagram 3.12

Cargo carried by air



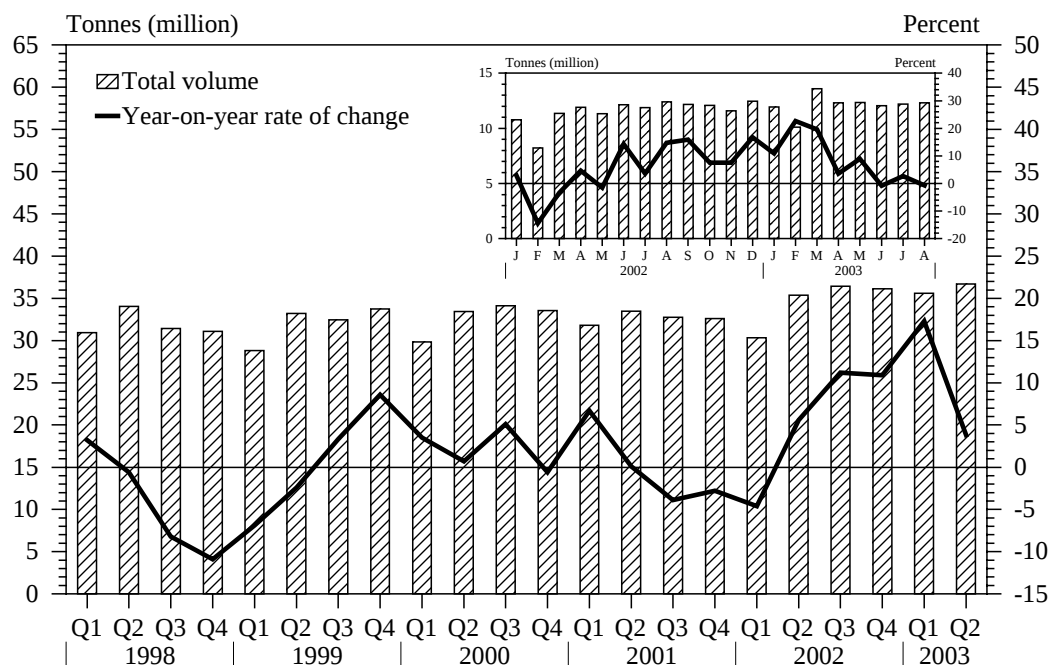
Note : (*) Provisional figures.

/3.34

3.34 On *ocean transport*, total *ocean cargo movements* amounted to 24.5 million tonnes in July-August 2003, up by only 1% from a year earlier, slower than the 4% rise in the second quarter. While transshipment cargo increased by 7%, direct shipment cargo fell by 3%. Within the total for July-August, inward ocean cargo fell by 1% to 16.0 million tonnes, while outward ocean cargo rose by 5% to 8.5 million tonnes. For the first eight months of 2003 as a whole, these two particular streams of cargo movement rose by 6% and 12% respectively over a year earlier, leading to an 8% rise in total ocean cargo movements. The corresponding increases in 2002 were all 6%.

Diagram 3.13

Cargo carried by sea



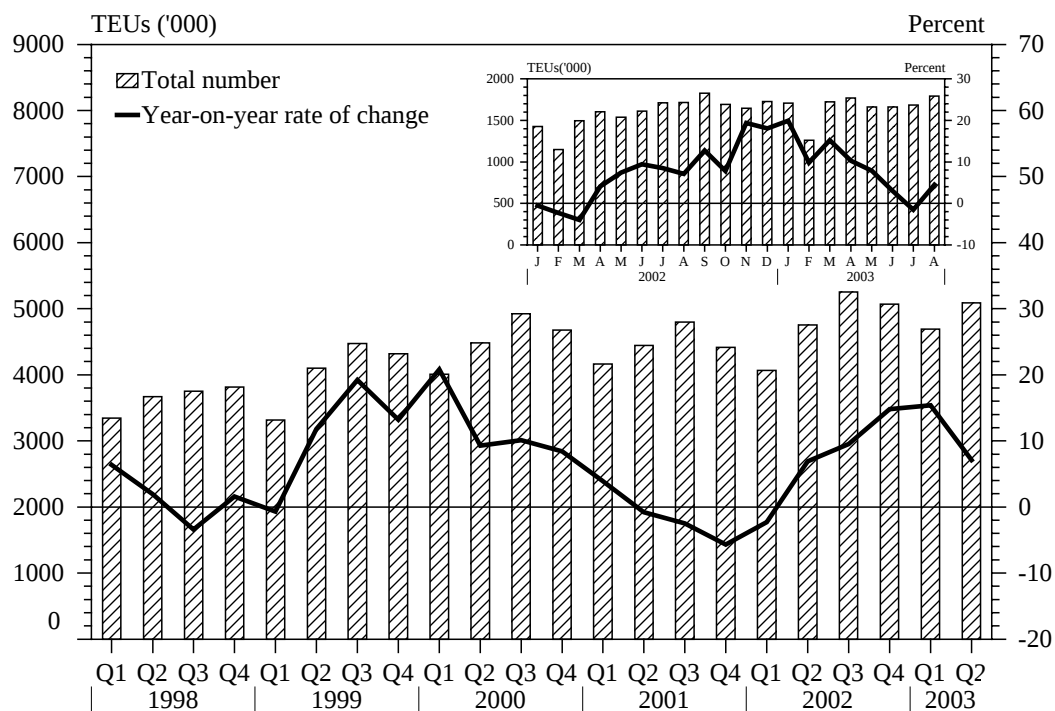
3.35 As to *container traffic*, total container throughput in terms of Twenty-foot Equivalent Units (TEUs) went up only slightly, by 1% over a year earlier to 3.5 million TEUs in July-August 2003, much moderated from the 7% rise in the second quarter. Within the total for July-August, inward container throughput, at 1.7 million TEUs, went up by 3% over a year earlier, while outward container throughput, at 1.8 million TEUs, was virtually unchanged. For the first eight months of 2003 as a whole, total container throughput rose by

/8%

8% over a year earlier, with inward and outward container throughput rising by 9% and 7% respectively. Concurrently, there was an on-going trend of manufactured products being shipped out directly from the nearby Mainland ports rather than indirectly through the Hong Kong port. Reflecting this, container throughput at the Yantian port soared further by 19% in the third quarter of 2003 over a year earlier, after a 26% surge in the second quarter.

Diagram 3.14

Container throughput



/Box 3.2

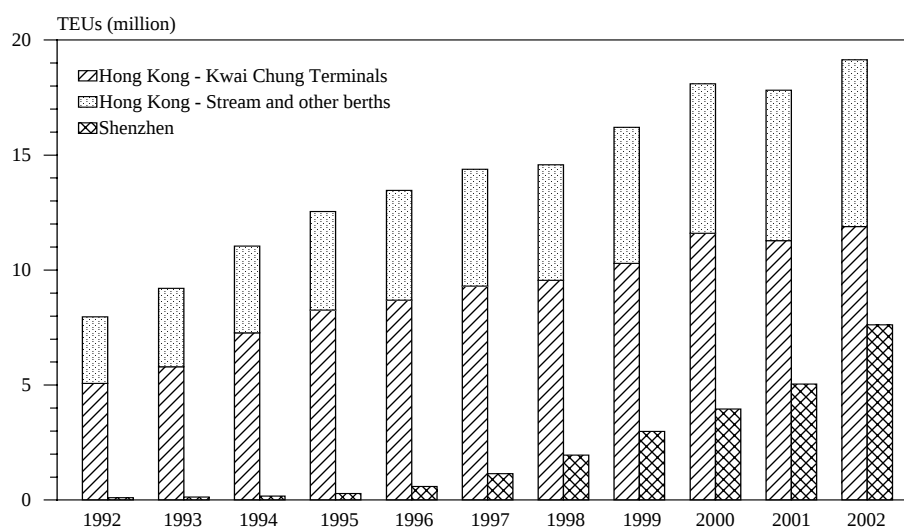
Box 3.2

Container throughput in Hong Kong and Shenzhen

The port of Hong Kong handled a total container throughput of 19.1 million TEUs in 2002, making it the world's busiest container port for nine of the past ten years. A major part of the container cargo handled by the Hong Kong port is either originated from or destined for the Pearl River Delta (PRD) region, which is Hong Kong's primary economic hinterland and extended production base.

However, the status of Hong Kong as the most important gateway for freight transport in South China is being increasingly impinged upon by the rapid development of the container ports in Shenzhen, specifically those in Yantian, Shekou and Chiwan. In 2002, the Shenzhen ports handled a total container throughput of 7.6 million TEUs. Over the past five years, container throughput in Shenzhen grew rapidly, at an average annual rate of 46%. This was much faster than the corresponding average annual growth rate of 6% for container throughput in Hong Kong. These differential growth trends continued in the first eight months of 2003, with container throughput in Shenzhen soaring by 40% over a year earlier, yet with that in Hong Kong up by only 8%. This mainly reflected the improvement in quality and capability of freight handling services as well as the streamlined customs procedures in the PRD region over the recent years. Relatively lower costs for the services in Shenzhen were also highly relevant. These factors are inducing more and more manufactured goods produced in the PRD region being shipped out directly from the ports in Shenzhen rather than indirectly through Hong Kong.

Growth in container throughput in Hong Kong and Shenzhen



Hong Kong's container port will continue to benefit from the rapid expansion of the Mainland economy and the PRD region. But it is likely to get a progressively smaller share of a much larger pie. Against this background, it is important to uphold the efficiency and competitiveness of Hong Kong's container port, as a pivotal facility in Hong Kong's broader trading and logistics sector.

/Tourism

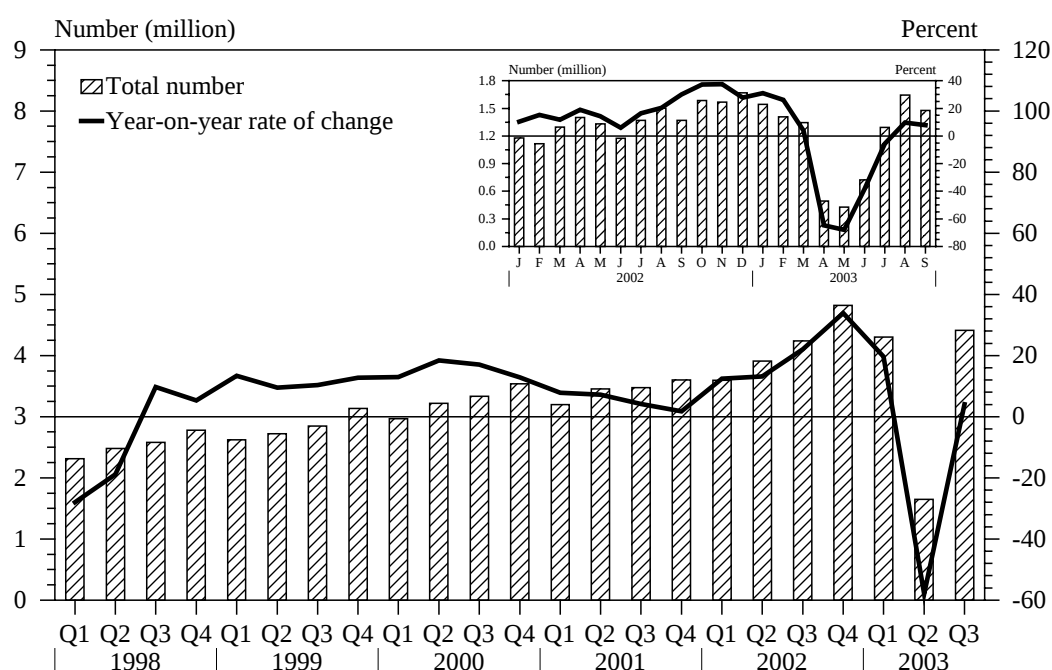
Tourism

3.36 After a severe set-back in the second quarter due to the SARS impact, inbound tourism showed a distinct recovery in the third quarter, particularly in August and September. The promotion campaigns conducted by the industry together with the Government, coupled with launch of the “individual visit” scheme for Mainland residents coming to Hong Kong⁽¹¹⁾, were the main contributory factors. The total number of *incoming visitors* rose by 4% over a year earlier to 4.4 million in the third quarter of 2003, comprising still a 6% decrease in July and then distinctly increases by 10% and 8% respectively in August and September. This followed a precipitous decline of 58% in the second quarter. For the first nine months of 2003 as a whole, the total number of incoming visitors declined by 12% over a year earlier, in stark contrast to the 21% rise in 2002.

3.37 Analysed by major source, visitors from the Mainland surged strongly, by 32% in the third quarter of 2003 over a year earlier. On the other hand, visitors from other major sources remained on a decline. Visitors from Japan, the United Kingdom, the United States, South and Southeast Asia, and Taiwan all fell, by 36%, 22%, 19%, 16% and 8% respectively.

Diagram 3.15

Number of incoming visitors



/Table 3.15

Table 3.15**Number of incoming visitors by place of residence
(year-on-year rate of change (%))**

	<u>2002</u>					<u>2003</u>		
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
All sources	21	12	13	22	34	20	-58	4
Mainland of China	53	42	44	55	68	53	-26	32
Taiwan	*	-1	-7	4	6	-3	-74	-8
South and Southeast Asia	9	-2	5	12	18	*	-81	-16
Japan	4	-8	-1	4	26	-2	-86	-36
United States	7	*	-1	5	25	-7	-84	-19
United Kingdom	5	2	*	4	14	2	-78	-22
Others	6	4	3	3	14	1	-72	-14

Notes : Figures shown in this table include also non-Macau residents coming to Hong Kong via Macau.

(*) Change of less than 0.5%.

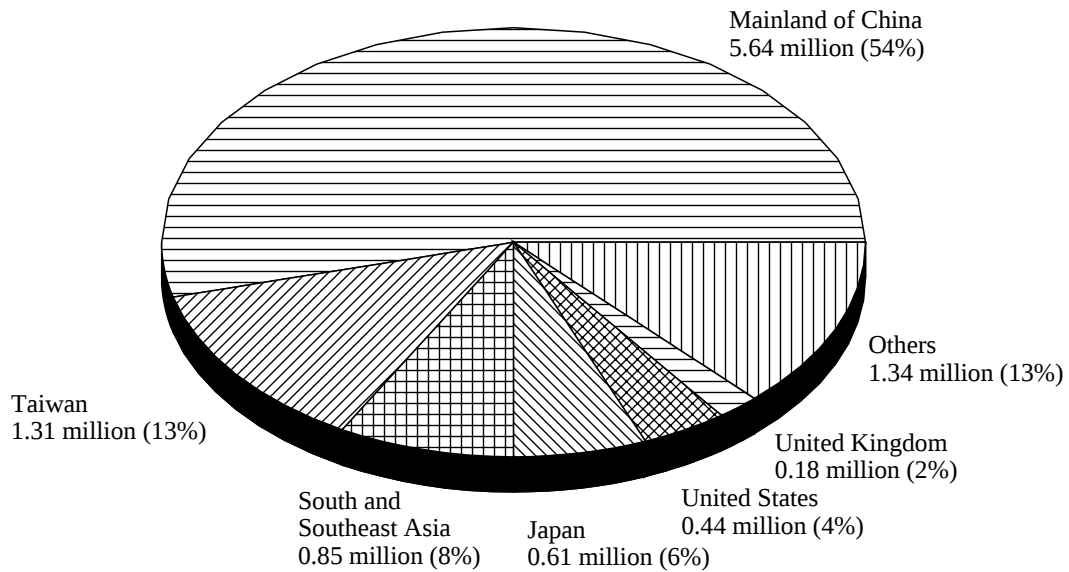
Source : Hong Kong Tourism Board.

3.38 The Mainland continued to be the largest source of visitors to Hong Kong, with a share of 54% in the first nine months of 2003. Taiwan came next (with a share of 13%), followed by South and Southeast Asia (8%), Japan (6%), the United States (4%), and the United Kingdom (2%).

/Diagram 3.16

Diagram 3.16

**Number of incoming visitors by source
in the first nine months of 2003**



Total number of incoming visitors in the first nine months of 2003 : 10.36 million

3.39 As at end-September 2003, there were 42 848 *hotel rooms* in Hong Kong, little changed from a year earlier. Along with the revival in inbound tourism, the *average hotel room occupancy rate*, rebounded sharply, to 80% in the third quarter of 2003, from that of 25% in the second quarter. Yet this was still lower than the level of 83% in the third quarter of 2002.

/Table 3.16

Table 3.16**Stock of hotel rooms and occupancy rate**

		Number of hotel rooms as at end of period [#]		Average hotel room occupancy rated during the period (%)
2002	Annual	43 634	(--)	84
	Q1	41 829	(--)	81
	Q2	42 747	(--)	83
	Q3	42 758	(--)	83
	Q4	43 634	(--)	89
2003	Q1	42 792	(2)	81
	Q2	42 818	(*)	25
	Q3	42 848	(*)	80

Notes : (#) As from the first quarter of 2002, this data series has a wider coverage, including all hotels and tourist guest houses on the record of the Office of the Licensing Authority in the Home Affairs Department. As such, the data for the first quarter of 2002 onwards are not directly comparable to those in the earlier periods.

() % change over a year earlier.

(*) Change of less than 0.5%.

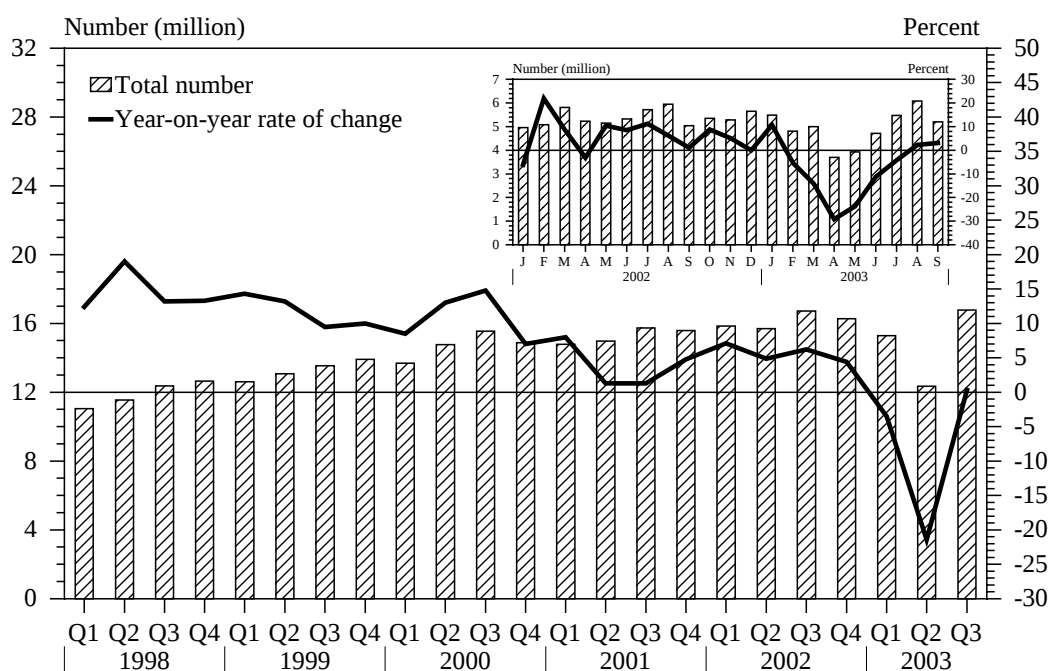
(--) Not applicable.

Source : Hong Kong Tourism Board.

/3.40

3.40 On *Hong Kong residents travelling abroad*, the total number of resident departures in the third quarter of 2003, at 16.8 million, were the same as a year earlier. This improved much from the 21% dip in the second quarter. As the SARS impact waned, the greater price discounts that continued to be offered by the travel agencies and the airlines also helped stimulate outbound travel. For the first nine months of 2003 as a whole, the total number of resident departures fell by 8% over a year earlier, as against the 6% rise in 2002. Analysed by major destination, resident departures to Australia and New Zealand and to Americas declined the most, both by 14% in the third quarter of 2003 over a year earlier, while resident departures to Taiwan fell by 7%. On the other hand, resident departures to South and Southeast Asia, Europe, Macau and North Asia ascended by 15%, 4%, 3% and 2% respectively. Resident departures to the Mainland remained stable.

Diagram 3.17
Number of Hong Kong resident departures



/Table 3.17

Table 3.17

**Number of Hong Kong resident departures by destination
(year-on-year rate of change (%))**

	<u>2002</u>					<u>2003</u>		
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
All destinations	6	7	5	6	4	-4	-21	*
Mainland of China	7	9	7	7	5	-3	-21	*
Macau	-3	-3	-5	*	-2	-7	-15	3
South and Southeast Asia	-3	-2	-11	1	-1	-10	-14	15
North Asia	2	5	-7	3	6	-18	-21	2
Americas ^(a)	-8	-14	-20	-6	18	-7	-54	-14
Taiwan	2	20	-10	-3	5	-4	-76	-7
Europe	7	10	*	8	13	-11	-30	4
Australia and New Zealand	-6	-8	-16	-2	2	-7	-8	-14
Others	-16	-40	-24	-2	35	-21	-20	5

Notes : (a) This includes the United States, Canada, Central America and South America.

(*) Change of less than 0.5%.

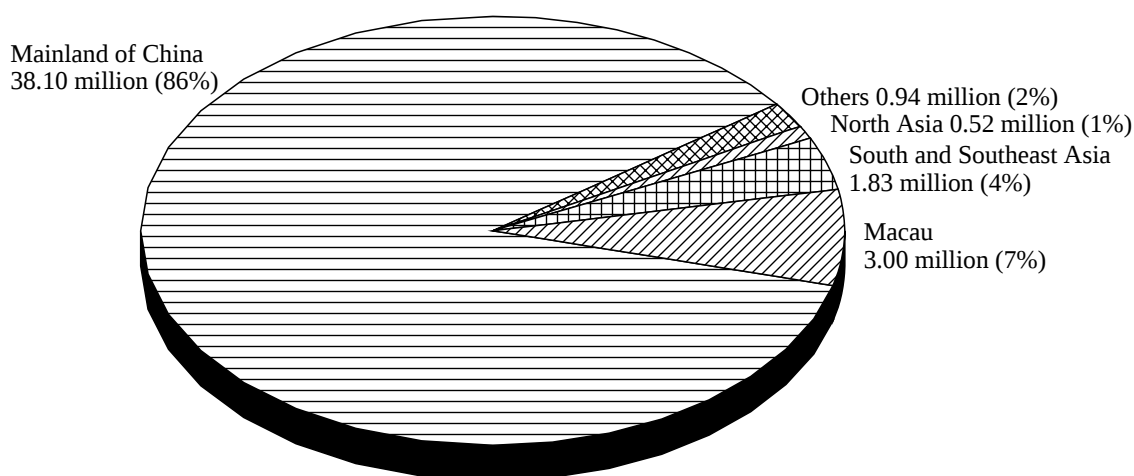
Source : Hong Kong Tourism Board.

3.41 The Mainland continued to be the most popular destination for Hong Kong resident departures, accounting for 86% of the total outbound trips in the first nine months of 2003. Most of these trips were destined for Guangdong Province. Macau came next (with a share of 7%), followed by South and Southeast Asia (4%), North Asia (1%), Taiwan (1%) and Europe (1%).

/Diagram 3.18

Diagram 3.18

**Number of Hong Kong resident departures by destination
in the first nine months of 2003**



Total number of resident departures in the first nine months of 2003 : 44.40 million

Telecommunications

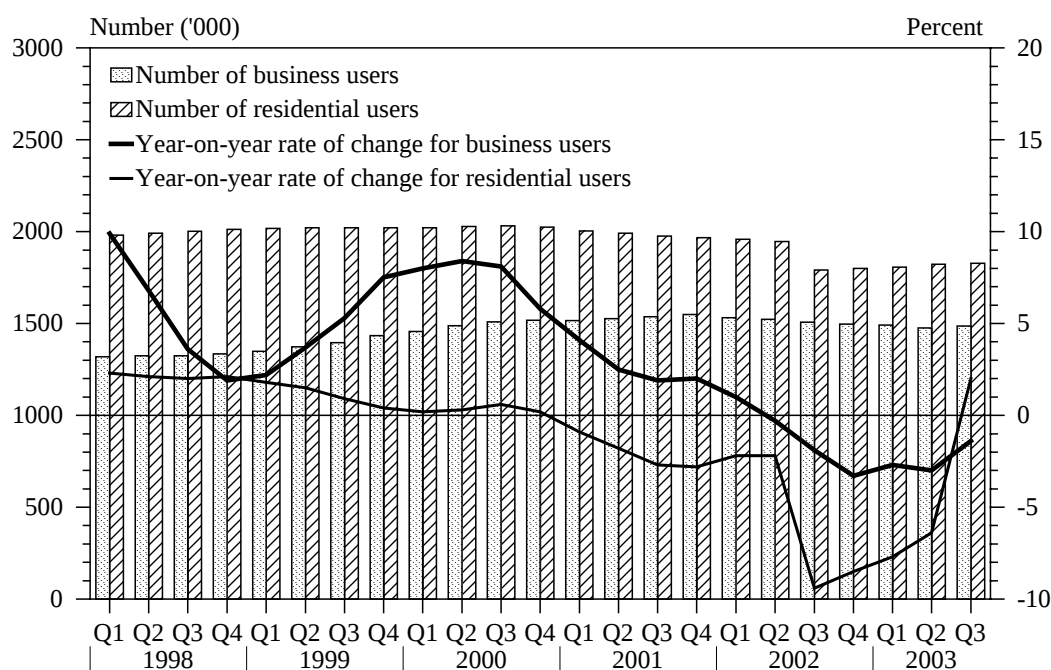
3.42 On *wireline services*, the total number of direct exchange lines continued to fall, by 1% over a year earlier to 3.81 million at end-September 2003. Within the total, the number of fixed telephone lines, at 3.31 million at end-September 2003, remained stable from a year earlier. While the number of fixed telephone lines for business customers decreased by 1% over a year earlier to 1.49 million, that for residential customers increased by 2% to 1.83 million. These two particular groups of customers accounted for 45% and 55% respectively of all the fixed telephone lines installed at end-September 2003. At 49 fixed telephone lines per 100 inhabitants, per capita tele-density in Hong Kong was amongst the highest in Asia. As regards the number of facsimile lines, it dropped by 11% over a year earlier to 499 700 at end-September 2003. At 30 facsimile lines per 100 business exchange lines, Hong

/Kong

Kong again ranked amongst the highest in Asia. On external telecommunications, external telephone traffic volume⁽¹²⁾ remained unchanged from a year earlier at 1 508 million minutes in the third quarter of 2003, reduced from the 2% increase in the second quarter. As to Internet usage, broadband services continued on a sharp uptrend, with the traffic volume soaring by 383% over a year earlier to 281 300 terabits in the third quarter of 2003. This came after a 315% leap in the second quarter. There was a further profound shift in Internet usage away from the public switch telephone network, where the traffic volume plummeted by 38% over a year earlier to 825 million minutes in the third quarter of 2003. The corresponding decline in the second quarter was 25%.

Diagram 3.19

**Number of fixed telephone lines* by main user category
(as at end of quarter)**

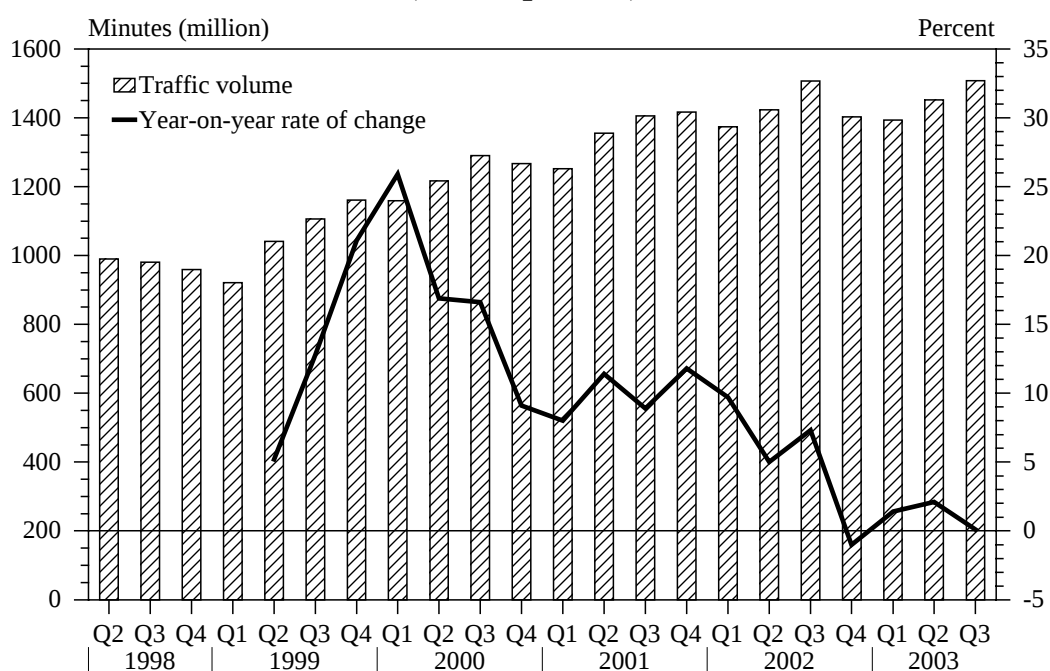


Note : (*) Not including facsimile lines.

/Diagram 3.20

Diagram 3.20

**External telephone traffic volume*
(in the quarter)**



Notes : Data prior to the second quarter of 1998 are not available.

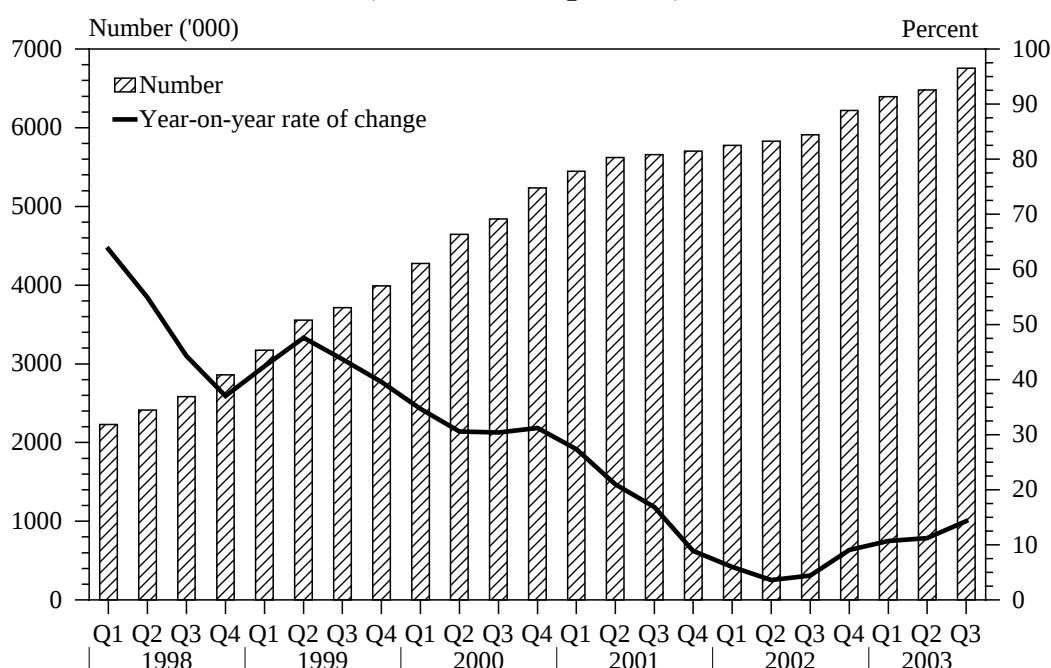
(*) Including access by international direct dialling (IDD) through telephone lines, facsimile lines and datel lines.

3.43 On *wireless services*, the mobile phone segment expanded further. The number of mobile phone customers went up further by 14% from a year earlier to 6.8 million at end-September 2003⁽¹³⁾. This corresponded to a mobile phone penetration rate of 99%, amongst the highest in the world. Meanwhile, the paging segment continued to shrink, with the number of paging customers declining further by 18% from a year earlier to 171 300 at end-September 2003.

/Diagram 3.21

Diagram 3.21

**Number of public mobile radiotelephone service customers*
(as at end of quarter)**



Note : (*) Including all mobile phone service subscribers and the stock of pre-paid Subscribed Identity Module (SIM) cards already sold to customers.

Notes :

- (1) On 1 August 2002, the Census and Statistics Department introduced a technical revision to the existing GDP series, as compiled from the expenditure approach. At the same time, a new data series on quarterly GDP by major economic sector at constant prices, backdated to the first quarter of 2000, was released. This new GDP series, as compiled from the production approach, enables analysis to be done of the value added contributions of the various economic sectors in real terms, in regard to their trend and relative significance.
- (2) The service sectors comprise the wholesale, retail and import/export trades, restaurants and hotels; transport, storage and communications; financing, insurance, real estate and business services; and community, social and personal services. In respect of contribution to GDP, the service sectors also include ownership of premises, which is analytically a service activity. Charges of financial intermediation are however deducted.

/(3)

- (3) The Index of Industrial Production is intended to reflect the recent trend of net output in real terms in the various local manufacturing industries. Output from outward processing operations across the boundary is not included.
- (4) The Monthly Survey of Orders-on-hand covers manufacturing firms engaging 50 or more workers. Its main purpose is to provide a broad indicator of the orders position in value terms in the local manufacturing sector at monthly intervals. Orders to be met by outward processing across the boundary are not included.
- (5) On 15 October 2003, the Secretary for Housing, Planning and Lands (SHPL) announced ways to further implement and consolidate the relevant policies and measures on the basis of the prevailing housing policy, as summarised below :
 - (a) In view of the decreasing supply of new flats in the next few years, the Application List System would be resumed as from January 2004, so that it could help regulate the demand for land through market forces to foster the healthy and normal development of the property market.
 - (b) Liaison with the two railway companies had been made to ensure that the dates of construction and completion of their property development projects would not generate significant impact on the market. The Kowloon-Canton Railway Corporation agreed that no residential developments along the West Rail and the Ma On Shan Rail would be completed before 2008. The Mass Transit Railway Corporation Limited undertook to review the planning for Tseung Kwan O Area 86, and it was anticipated that the first batch of flats from that project would not be completed until 2007 at the earliest.
 - (c) The periods of building covenant of development projects which originally were to expire between 1 November 2003 and 31 October 2004 would be extended for one year without additional charges, in order to provide developers with greater flexibility in adjusting the completion date and timing of sale of their development projects according to the market situation.
 - (d) All unsold and returned Home Ownership Scheme flats would not be offered for sale as subsidised housing before end-2006. For those flats already completed or still under construction but had never been offered for sale, the Housing Authority would actively explore various disposal options.
 - (e) On the Landlord and Tenant (Consolidation) Ordinance, the amendment Bill was submitted to the Legislative Council for consideration in June 2003. The Government would work hard to secure early passage of the Bill.

This was further to the announcement by SHPL on 13 November 2002. For details of that announcement, see Footnote (8) to Chapter 3 of the 2002 Economic Background.

- (6) Developers offered a variety of inducements including flexible payment terms, top-up loans, cash rebates, and mortgage subsidies in the early part of the repayment period. Flat buyers could opt for different combinations of these privileges, or else seek a direct price discount. In effect, the acquisition cost initially and/or the mortgage cost in the ensuing few years would be reduced for the flat buyers.

/(7)

- (7) Starting from 27 October 2003, persons with net assets under their control and disposal for investment of no less than \$6.5 million in permissible investment assets, including real estate and specified financial assets, can apply for admission into Hong Kong as capital investment entrants. This new policy, as part of the population policy announced on 26 February 2003, will be applied to all foreign nationals, Macao SAR residents and Taiwan residents, but not Mainland residents.
- (8) The Government operates an Application System under the Land Sale Programme as from April 1999, whereby additional sites are set aside on an Application List for open application by property developers. Provided that the minimum price offered by the applicant is acceptable to the Government, the site involved can be released from the Application List for open auction or tender. This renders a flexible supply of Government land in response to market demand.
- (9) Virtually all the land in Hong Kong is held on a leasehold basis. A predominant part of the existing developed and developable land is already in the private sector domain. In order to facilitate redevelopment in line with the town planning and urban renewal objectives, modification of usage (including modification by way of land exchange) may be granted by the Government to old leases of land upon application from the landlords. A land premium, equivalent to the difference in land value between the old and the new usage, is normally required for granting of the modification.
- (10) Of the 14 incubatees, ten were admitted in the third quarter of 2003, having admitted four in the second quarter. They were admitted under the Incu-Tech Programme run by the Hong Kong Science & Technology Parks Corporation, so as to assist eligible technology start-up ventures in their vulnerable inception stage.
- (11) With effect from 28 July 2003, residents of Dongguan, Zhongshan, Jiangmen and Foshan can travel to Hong Kong under the “individual visit” scheme. The scheme has been extended to residents of Guangzhou, Shenzhen, Zhuhai and Huizhou on 20 August 2003, and to residents of Beijing and Shanghai on 1 September 2003. Residents in these cities can apply for travel documents which allow them to make two visits within a period of three months, and to stay in Hong Kong each time for up to seven days. The scheme will be extended further to all residents of Guangdong by 1 May 2004.
- (12) This includes access by international direct dialling (IDD) through telephone lines, facsimile lines and datel lines.
- (13) This figure includes all mobile phone service subscribers and the stock of pre-paid Subscribed Identity Module (SIM) cards already sold to customers.

CHAPTER 4 : THE FINANCIAL SECTOR*

Overall financial market situation

4.1 The Hong Kong dollar spot exchange rate strengthened during the third quarter of 2003, and the spread of the twelve-month Hong Kong dollar forward rate against the spot rate switched from a premium to a discount. There was an increased demand for Hong Kong dollar assets, induced by optimism about the improved performance and near-term outlook of the Hong Kong economy as well as by the weakening US dollar against currencies in the region. Reportedly, there was also an unwinding of short Hong Kong dollar positions by some business operators. In response to market offers, the Hong Kong Monetary Authority (HKMA) sold HK\$0.5 billion for an equivalent amount of US dollars on 23 September. On the monetary aggregates, narrow money supply continued to grow at a faster pace than broader money supply during the third quarter, while the demand for domestic credit stayed largely subdued. As a contraction in Hong Kong dollar loans went along with a further expansion in Hong Kong dollar deposits, the Hong Kong dollar loan-to-deposit ratio drifted further lower during the third quarter. As to the local stock market, share prices continued on a strong rally, on the back of better economic data and increased inflow of funds. The Hang Seng Index surged to a high at 11 296 on 24 September, before closing the month at 11 230, 17.3% above the level at end-June.

Exchange rates

4.2 The spot exchange rate of the Hong Kong dollar against the US dollar stayed on the strong side of the linked rate (at 7.80) throughout the third quarter of 2003. It appreciated more visibly towards the end of the quarter, reaching 7.749 on 23 September and hovering at around that level towards end-September. The spread of the twelve-month forward rate against the spot

(*) This chapter is jointly prepared by the Hong Kong Monetary Authority and the Economic Analysis Division.

rate switched from a premium to a discount of 105 pips (each pip equivalent to HK\$0.0001) also on 23 September. The discount narrowed to 79 pips at end-September, which contrasted with a premium of 120 pips at end-June. The fluctuations in the Hong Kong dollar exchange rate in the latter part of September were affected by more intense rumours for revaluation of the renminbi.

4.3 Under the linked exchange rate system⁽¹⁾, the movements in the exchange rates of the Hong Kong dollar against other major currencies follow closely those in the US dollar. During the third quarter of 2003, the US dollar weakened against most of the East Asian currencies, amidst concerns about the worsening US trade deficit. In particular, the yen - dollar rate fell by 2.8% from a monthly average of 118.3 in June to that of 115.0 in September. The US dollar also eased against the Thai baht, the Korean won and the New Taiwan dollar by 2.8%, 2.4% and 1.9% respectively. Yet it strengthened against the major European currencies. The dollar - euro rate appreciated by 3.5% from a monthly average of 1.167 in June to that of 1.130 in September, and the dollar - pound sterling rate by 2.8% from a monthly average of 1.661 to that of 1.614 between these two months.

4.4 Taking these currency movements together, the trade-weighted Nominal Effective Exchange Rate Index⁽²⁾ of the Hong Kong dollar went up marginally by 0.1%, from a monthly average of 100.56 in June to 100.63 in September. However, after adjusting for changes in the respective consumer price indices, the trade-weighted Real Effective Exchange Rate Index of the Hong Kong dollar was down by 2.2%, from 90.0 to 88.0 over the same period.

/Table 4.1

Table 4.1

**Trade-weighted Effective Exchange Rate Index
of the Hong Kong dollar**

<u>Average for the month</u>		<u>Trade-weighted Nominal EERI^(a) (Jan 2000 = 100)</u>		<u>Trade-weighted Real EERI^(b) (Jan 2000 = 100)</u>	
2002	Mar	105.9	(0.5)	99.3	(1.2)
	Jun	103.5	(-2.3)	95.5	(-3.8)
	Sep	103.0	(-0.5)	94.4	(-1.1)
	Dec	102.7	(-0.3)	93.3	(-1.2)
2003	Mar	101.8	(-0.9)	92.1	(-1.2)
	Jun	100.6	(-1.2)	90.0	(-2.3)
	Sep	100.6	(0.1)	88.0	(-2.2)

Notes : (a) The Nominal Effective Exchange Rate Index (EERI) of the Hong Kong dollar is a weighted average of the exchange rates of the Hong Kong dollar against the currencies of its major trading partners, with the weights adopted being the respective shares of these trading partners in the total value of merchandise trade for Hong Kong.

As from 2 January 2002, a new series of nominal EERI replaces the old series, with the weights updated to reflect the average pattern of merchandise trade during 1999 and 2000, and with the base period brought up to January 2000.

The currency basket of the new series has also been updated to include the euro and the Philippine peso, and to exclude the five currencies pertaining to the participating countries of the euro.

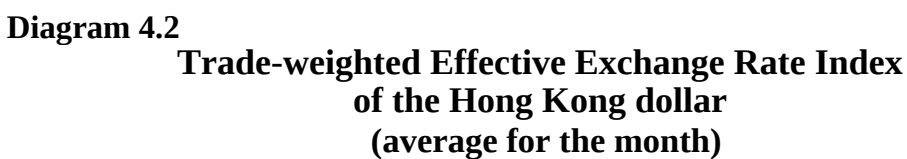
(b) The Real Effective Exchange Rate Index of the Hong Kong dollar is obtained by adjusting the Nominal EERI for relative movements in the seasonally adjusted consumer price indices of the respective trading partners.

() % change over three months earlier.

Positive change in the EERI denotes appreciation of the Hong Kong dollar; negative change in the EERI denotes depreciation.

/Diagram 4.1

**Exchange rate of the Hong Kong dollar against the US dollar
(average for the month)**



Interest rates

4.5 Higher liquidity in the banking sector resulting from increased inflow of funds pushed down the local inter-bank interest rates during the third quarter of 2003. At end-September, the three-month HIBOR closed at 0.7%, down from 1.0% at end-June. Over the same period, the negative spread of the three-month HIBOR against the corresponding Euro-dollar deposit rate widened from six basis points to 44 basis points.

4.6 As the US Fed Funds target rate stayed intact at 1% in the third quarter of 2003, the Base Rate under the Discount Window operated by HKMA also held steady, at 2.5%. The best lending rate and savings deposit rate offered by the major commercial banks likewise remained unchanged, at 5.00% and 0.03% respectively throughout the quarter. There was a marginal widening in the spread of the best lending rate over the three-month time deposit rate, from an average of 4.91 percentage points in the second quarter of 2003 to 4.92 percentage points in the third quarter.

4.7 Intensified competition amongst the banks for residential mortgage business continued to hold down the cost of home financing, especially on flats sold in the primary market. In September, 92.9% of the new residential mortgages were granted at more than two percentage points below the best lending rate, further up from the share of 92.0% in June⁽³⁾.

/Diagram 4.3

Interest rates

The graph displays three interest rate series over time. The Y-axis represents the rate in percent per annum, ranging from 0 to 12. The X-axis shows months from May 1998 to September 2003. The 'Base Rate under the Discount Window' (thick black line) starts at 7%, peaks at 8% from January 2000 to December 2000, and then declines to 2.5% by September 2003. The 'Overnight HIBOR' (thin black line) is highly volatile, peaking at nearly 10% in August 1998 and fluctuating between 3.5% and 7% for much of the period. The 'Overnight Euro-dollar deposit rate' (gray line) is also volatile, generally tracking between 4.5% and 6.5% until early 2001, after which it declines to around 1% by late 2003.

Month	Overnight HIBOR (%)	Base Rate under the Discount Window (%)	Overnight Euro-dollar deposit rate (%)
May 1998	7.0	7.0	5.5
Aug 1998	9.8	7.0	5.5
Dec 1998	4.5	6.2	5.0
Jun 1999	4.5	6.2	5.0
Dec 1999	3.5	7.0	5.5
Jun 2000	6.5	8.0	6.5
Dec 2000	6.5	8.0	6.5
Jun 2001	4.5	5.5	4.5
Dec 2001	3.5	3.2	1.8
Jun 2002	1.5	3.2	1.5
Dec 2002	1.2	2.8	1.2
Jun 2003	1.0	2.5	1.0
Sep 2003	0.8	2.5	0.8

The graph displays two interest rate series over a five-year period. The Y-axis, labeled 'Percent per annum', ranges from 0 to 14 in increments of 2. The X-axis shows time in months, with labels for March (M), June (J), September (S), and December (D) for each year from 1998 to 2003. The 'Three-month HIBOR' is represented by a thin line, and the 'Three-month Euro-dollar deposit rate' is represented by a thick line. Both rates show significant volatility in 1998 and 1999, with peaks around 12% for HIBOR and 6% for Euro-dollar. From 2000 onwards, both rates show a steady decline, with the HIBOR rate generally remaining slightly above the Euro-dollar rate until late 2002, after which they converge and both drop below 2% by the end of 2003.

Year	Month	Three-month HIBOR (%)	Three-month Euro-dollar deposit rate (%)
1998	Mar	9.5	5.8
1998	Jun	6.5	5.6
1998	Sep	11.8	5.6
1998	Dec	5.5	5.2
1999	Mar	5.2	4.8
1999	Jun	5.0	4.8
1999	Sep	6.5	5.5
1999	Dec	6.0	6.0
2000	Mar	5.8	6.0
2000	Jun	6.8	6.8
2000	Sep	6.5	6.5
2000	Dec	5.8	6.5
2001	Mar	5.0	5.5
2001	Jun	3.8	3.8
2001	Sep	3.5	3.5
2001	Dec	2.0	1.8
2002	Mar	2.2	2.0
2002	Jun	1.8	1.8
2002	Sep	1.8	1.8
2002	Dec	1.5	1.5
2003	Mar	1.2	1.2
2003	Jun	1.0	1.0
2003	Sep	1.0	1.0
2003	Dec	1.0	1.0

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Diagram 4.3 (cont'd)

**(c) Twelve-month HIBOR and Euro-dollar deposit rate
(average for the month)**

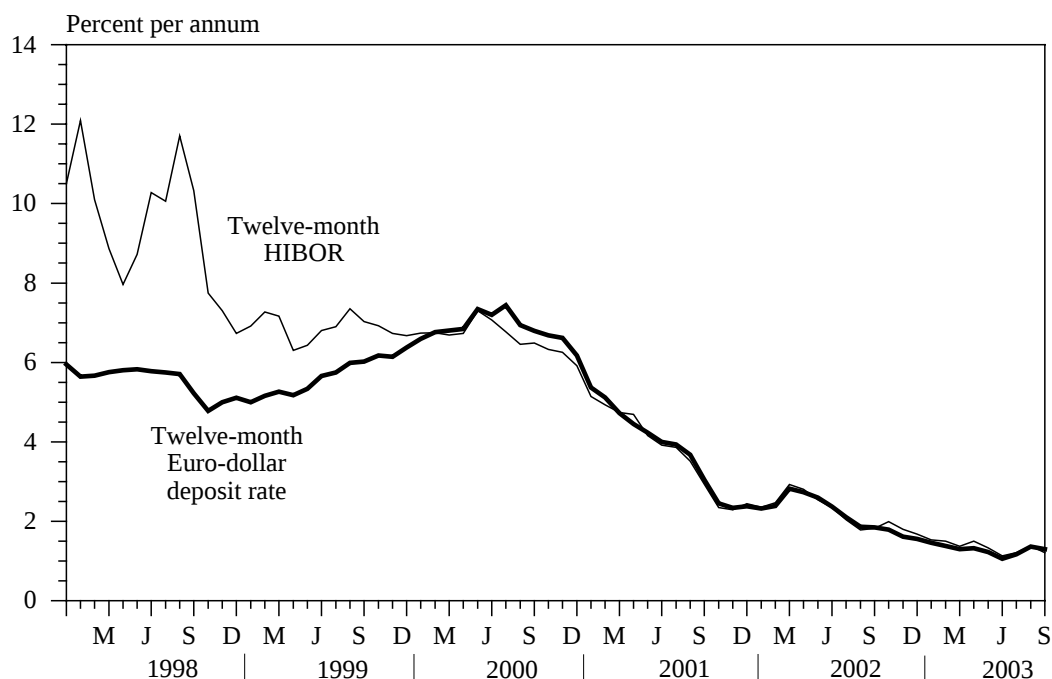


Table 4.2

**Hong Kong dollar inter-bank offer rates (HIBORs)
(% per annum)**

Average for the month		Overnight HIBOR		Three-month HIBOR		Twelve-month HIBOR	
2002	Mar	1.86	(9)	2.12	(17)	2.93	(11)
	Jun	1.41	(-35)	1.75	(-9)	2.34	(-4)
	Sep	1.67	(-11)	1.77	(*)	1.82	(-3)
	Dec	1.16	(-13)	1.48	(10)	1.68	(12)
2003	Jan	1.18	(-9)	1.36	(4)	1.54	(7)
	Feb	1.20	(-7)	1.34	(4)	1.50	(12)
	Mar	1.17	(-11)	1.28	(5)	1.37	(7)
	Apr	1.29	(1)	1.41	(15)	1.50	(18)
	May	1.14	(-12)	1.30	(6)	1.33	(11)
	Jun	1.06	(-18)	1.06	(1)	1.13	(8)
	Jul	0.96	(-7)	1.08	(1)	1.21	(4)
	Aug	0.88	(-14)	1.08	(-1)	1.38	(1)
	Sep	0.64	(-39)	0.94	(-16)	1.21	(-9)

Notes : () Figures in brackets represent the spread between the HIBOR and the corresponding Euro-dollar deposit rate in basis point. A positive value denotes a differential in favour of the Hong Kong dollar, while a negative value denotes a differential in favour of the US dollar.

(*) Spread of less than one basis point.

/Table 4.3

Table 4.3

Hong Kong dollar deposit and lending rates
 (% per annum, as average of the rates
 quoted by the major banks)

		Interest rates on time deposits below HK\$100,000					Savings deposit rate	Best lending rate
<u>Average for the month</u>		<u>One- week</u>	<u>One- month</u>	<u>Three- month</u>	<u>Six- month</u>	<u>Twelve- month</u>		
2002	Mar	0.21	0.55	0.62	0.84	1.39	0.16	5.13
	Jun	0.17	0.29	0.36	0.46	0.74	0.16	5.13
	Sep	0.16	0.33	0.38	0.40	0.43	0.16	5.13
	Dec	0.09	0.13	0.15	0.19	0.25	0.03	5.00
2003	Jan	0.08	0.10	0.11	0.16	0.21	0.03	5.00
	Feb	0.08	0.08	0.09	0.14	0.19	0.03	5.00
	Mar	0.08	0.09	0.09	0.12	0.17	0.03	5.00
	Apr	0.08	0.09	0.10	0.13	0.17	0.03	5.00
	May	0.08	0.08	0.09	0.12	0.14	0.03	5.00
	Jun	0.08	0.08	0.08	0.09	0.10	0.03	5.00
	Jul	0.07	0.08	0.08	0.09	0.10	0.03	5.00
	Aug	0.07	0.08	0.08	0.09	0.12	0.03	5.00
	Sep	0.07	0.07	0.07	0.08	0.10	0.03	5.00

Deposits and money supply

4.8 Hong Kong dollar deposits (adjusted to include foreign currency swap deposits)⁽⁴⁾ rose further by 2.4% during the third quarter of 2003 to \$1,886 billion at end-September, following a 2.1% increase during the second quarter. At end-September, Hong Kong dollar deposits accounted for 54.9% of total deposits, marginally less than the proportion of 55.0% at end-June. On a year-on-year comparison, Hong Kong dollar deposits rose by 3.6% at end-September 2003.

/4.9

4.9 Within the total Hong Kong dollar deposits, demand deposits kept increasing strongly, by 12.0% during the third quarter of 2003, further to a 10.7% surge during the second quarter. Savings deposits also went up, albeit more moderately, by 6.6% and 5.4% respectively during the second and third quarters. On the other hand, time deposits went down, by 2.3% and 1.6% respectively during the two quarters. This pointed to a sustained shift in the composition of Hong Kong dollar deposits more towards those of higher liquidity under the prevailing low interest rate environment. Greater transaction demand for cash or near-cash money, in line with the pick-up in business activity, also contributed. The compositional shift was even more apparent on a year-on-year comparison, with demand and savings deposits surging by 33.1% and 22.0% respectively but with time deposits dipping by 11.3% at end-September 2003.

Table 4.4

Hong Kong dollar deposits with authorized institutions

% change during the quarter		Demand deposits	Savings deposits	Time deposits ^{(a)(b)}	Total Hong Kong dollar deposits ^(a)
2002	Q1	-4.9	0.5	-1.9	-1.3
	Q2	3.6	3.9	-1.0	1.0
	Q3	4.7	-0.9	-2.5	-1.5
	Q4	10.5	6.2	-4.7	0.2
2003	Q1	-2.9	2.2	-3.2	-1.2
	Q2	10.7	6.6	-2.3	2.1
	Q3	12.0	5.4	-1.6	2.4
Total amount at the end of September 2003 (HK\$Bn)		176	775	935	1,886
% change over a year earlier		33.1	22.0	-11.3	3.6

Notes : (a) Adjusted to include foreign currency swap deposits.

(b) Time deposits with licensed banks plus deposits with restricted licence banks and deposit-taking companies.

/4.10

4.10 Total foreign currency deposits (adjusted to exclude foreign currency swap deposits) went up by 2.6% during the third quarter of 2003 to \$1,547 billion at end-September, faster than the 1.9% rise during the second quarter. This was mainly attributable to a rebound in non-US dollar deposits, from a 2.1% decline to a 5.3% rise, more than offsetting the concurrent slow-down in growth in US dollar deposits, from 4.0% to 1.3%. On a year-on-year comparison, total foreign currency deposits rose by 5.4% at end-September 2003, with US dollar deposits and non-US dollar deposits increasing by 6.6% and 3.1% respectively.

Table 4.5

Foreign currency deposits with authorized institutions

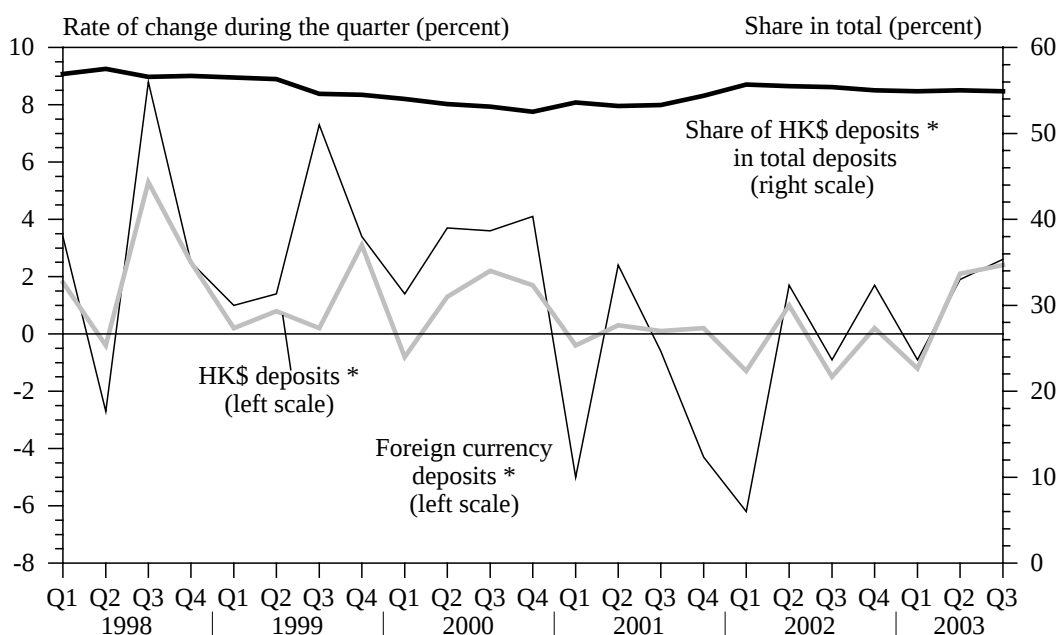
<u>% change during the quarter</u>		<u>US\$ deposits^(a)</u>	<u>Non-US\$ deposits^(a)</u>	<u>Total foreign currency deposits^(a)</u>	<u>Foreign currency swap deposits</u>
2002	Q1	-2.9	-12.7	-6.2	-6.9
	Q2	1.1	3.2	1.7	-8.0
	Q3	-3.3	4.2	-0.9	-7.5
	Q4	3.4	-1.6	1.7	-8.6
2003	Q1	-2.1	1.7	-0.9	-8.4
	Q2	4.0	-2.1	1.9	-7.2
	Q3	1.3	5.3	2.6	-6.6
Total amount at the end of September 2003 (HK\$Bn)		1,045	502	1,547	2
% change over a year earlier		6.6	3.1	5.4	-27.4

Note : (a) Adjusted to exclude foreign currency swap deposits.

/Diagram 4.4

Diagram 4.4

**Deposits with authorized institutions
by currency denomination and
share of Hong Kong dollar deposits in total deposits**



Note : (*) Adjusted for foreign currency swap deposits.

4.11 Total deposits with authorized institutions in Hong Kong expanded further by 2.5% during the third quarter of 2003 to \$3,433 billion at end-September, having risen by 2.0% during the second quarter. This was entirely due to a 2.5% gain in deposits with licensed banks during the third quarter of 2003, after a 2.0% rise during the second quarter. Such deposits constituted 98.8% of the total deposits with authorized institutions at end-September. On the other hand, deposits with restricted licence banks and deposit-taking companies decreased by 2.8% and 5.4% respectively during the third quarter, reversing the increases of 4.6% and 0.9% during the second quarter. A similar pattern of change was observed on a year-on-year comparison. Deposits with licensed banks went up by 4.6% at end-September 2003, whereas deposits with restricted licence banks and deposit-taking companies shrank by 10.6% and 8.4% respectively. Taken together, there was a 4.4% rise in total deposits.

/Table 4.6

Table 4.6**Total deposits by major type of authorized institution**

		<u>With licensed banks</u>				<u>With restricted licence banks</u>	<u>With deposit- taking companies</u>	
<u>% change during the quarter</u>		<u>Demand deposits</u>	<u>Savings deposits</u>	<u>Time deposits</u>	<u>Sub- total</u>	<u>Time deposits</u>	<u>Time deposits</u>	<u>Total</u>
2002	Q1	-1.5	0.2	-5.0	-3.5	-3.0	-7.0	-3.5
	Q2	4.4	4.4	-0.2	1.2	10.6	-3.0	1.3
	Q3	2.2	0.3	-2.2	-1.3	7.7	-2.2	-1.2
	Q4	10.9	6.1	-1.9	1.0	-6.9	3.3	0.9
2003	Q1	-0.6	3.3	-2.9	-1.0	-5.5	-7.0	-1.0
	Q2	11.0	5.5	-0.4	2.0	4.6	0.9	2.0
	Q3	12.4	6.4	-0.4	2.5	-2.8	-5.4	2.5
Total amount at the end of September 2003 (HK\$Bn)		226	1,098	2,069	3,394	34	5	3,433
% change over a year earlier		37.6	23.1	-5.4	4.6	-10.6	-8.4	4.4

4.12 Narrow money supply continued to grow at a faster pace than broader money supply. Specifically, HK\$M1⁽⁵⁾, as narrow money supply, surged by 7.9% during the third quarter of 2003 to \$299 billion at end-September, further to a 6.4% rise during the second quarter. On a seasonally adjusted basis, HK\$M1 also rose visibly, by 8.7% and 7.2% respectively during the second and third quarters⁽⁶⁾. HK\$M2 and HK\$M3 (adjusted to include foreign currency swap deposits), as broader money supply, had much smaller increases, by 2.2% and 2.0% respectively during the third quarter of 2003 to \$2,056 billion and \$2,072 billion at end-September. These followed corresponding gains of 2.2% and 2.1% during the second quarter. On a year-on-year comparison, HK\$M1 soared by 23.7% at end-September 2003, again much exceeding the increases in HK\$M2 and HK\$M3 by 4.1% and 3.9% respectively. Apart from the greater transaction demand for liquid money brought about by the pick-up in business activity, the low return on interest-bearing deposits relative to other financial assets was also a major factor contributing to the slower growth in broader money supply.

/Table 4.7

Table 4.7**Hong Kong dollar money supply and total money supply**

% change during the quarter		<u>M1</u>			<u>M2</u>		<u>M3</u>	
		<u>HK\$</u>		<u>Total</u>	<u>HK\$^(a)</u>	<u>Total</u>	<u>HK\$^(a)</u>	<u>Total</u>
2002	Q1	-0.1	(0.5)	1.5	-1.0	-3.1	-1.0	-3.1
	Q2	1.7	(5.4)	2.4	1.2	1.7	1.2	1.7
	Q3	3.5	(2.9)	2.1	-1.4	-0.8	-1.3	-0.7
	Q4	7.3	(3.4)	8.0	0.4	1.4	0.5	1.3
2003	Q1	0.4	(2.7)	1.4	-0.8	-0.3	-0.8	-0.4
	Q2	6.4	(8.7)	7.1	2.2	2.2	2.1	2.2
	Q3	7.9	(7.2)	8.7	2.2	2.4	2.0	2.4
Total amount at the end of September 2003 (HK\$Bn)		299	(303)	349	2,056	3,671	2,072	3,712
% change over a year earlier		23.7	(23.8)	27.5	4.1	5.8	3.9	5.6

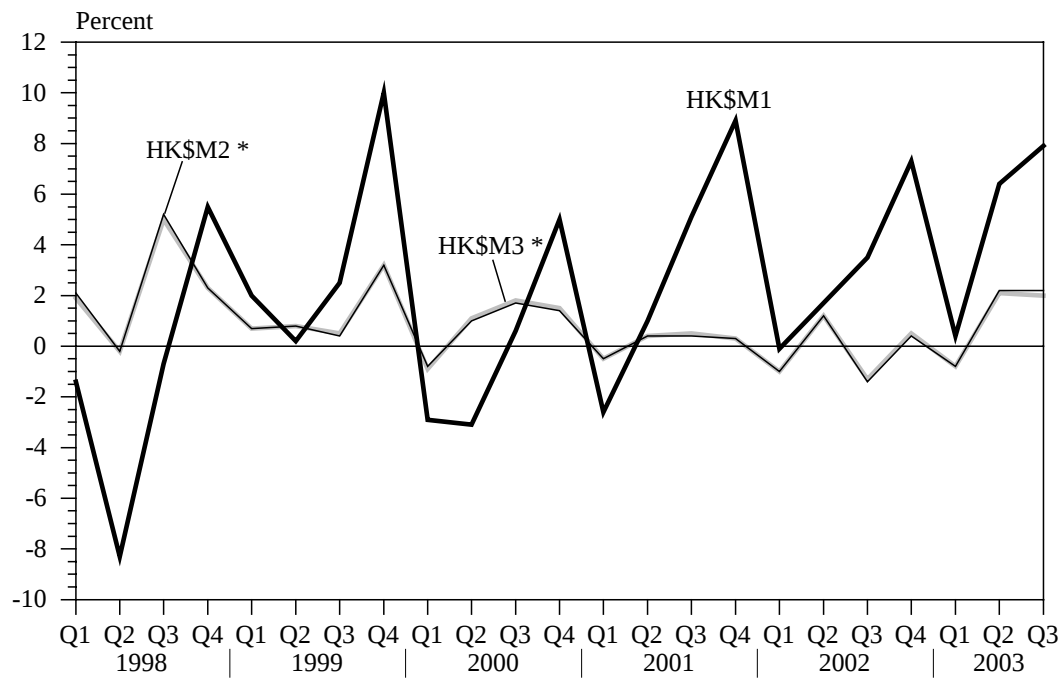
Notes : () Figures in brackets represent percentage changes on the basis of the seasonally adjusted series of HK\$M1. Seasonality is not apparent for the other monetary aggregates.

(a) Adjusted to include foreign currency swap deposits.

/Diagram 4.5

Diagram 4.5

**Hong Kong dollar money supply
(rate of change during the quarter)**



Note : (*) Adjusted to include foreign currency swap deposits.

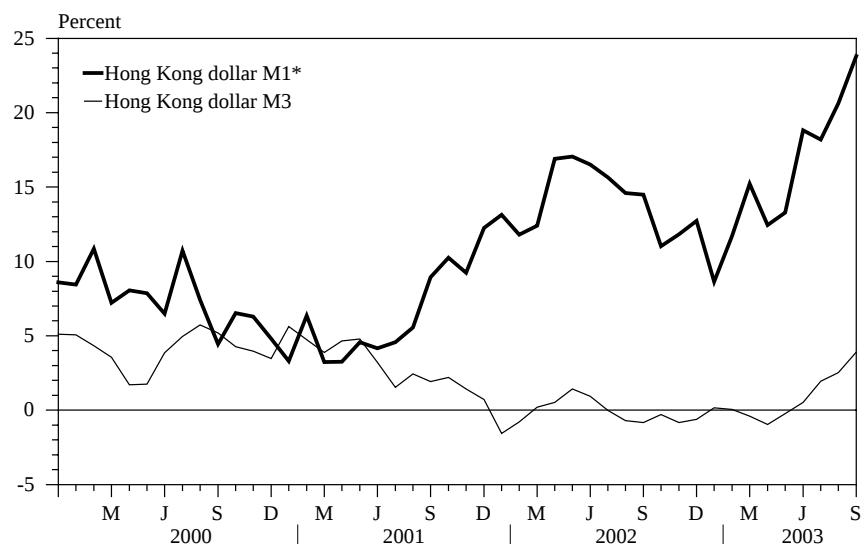
/Box 4.1

Box 4.1

Divergent movement between the Hong Kong dollar narrow and broad money supply

HK\$M1, as an indicator of narrow money supply, has increased much faster than HK\$M3, as an indicator of broad money supply, by 48.5% as against 3.5% since mid-2001.

Monetary aggregates
(year-on-year rate of change)



Note : (*) Seasonally adjusted.

The following factors may have contributed to this divergent movement. *First*, interest rates have fallen continuously in recent years. Specifically, interest rates on savings deposits and three-month time deposits have both dropped from around 5% in late 2000 to near zero at present. This has reduced the cost of holding non-interest-bearing cash or demand deposits, as well as caused some portfolio shift away from broad money. *Secondly*, the increasing economic links between Hong Kong and the Mainland have raised the demand for Hong Kong dollar currency. This is particularly so upon implementation of the “individual visit” scheme for Mainland visitors to Hong Kong, and upon a relaxation of the limit to the amount of cash allowed to be carried by individuals when travelling abroad. *Thirdly*, the surge in local stock market activity since April has also led to an accelerated growth in Hong Kong dollar demand deposits.

A study by HKMA shows a stable relationship between GDP, broad money and the opportunity cost of holding money. Other things being equal, a 1% rise in real GDP would raise real money demand by 1.7% in the long run, whereas a 1 percentage point rise in the opportunity cost of holding money would reduce money balances by 4.2%.

/Hong

Hong Kong dollar external claims and liabilities of authorized institutions

4.13 Hong Kong dollar claims held by Hong Kong's authorized institutions on banks outside Hong Kong went up by 34.1% over end-2002 to \$248.8 billion at end-August 2003. On a year-on-year comparison, the increase was 32.4% at end-August 2003. This was partly due to increased placements with banks in Europe and the Mainland. On the other hand, Hong Kong dollar liabilities owed by Hong Kong's authorized institutions to banks outside Hong Kong contracted by 21.7% over end-2002 to \$126.2 billion at end-August 2003. On a year-on-year comparison, there was a decrease of 22.7% at end-August 2003. Taken together, Hong Kong's authorized institutions had net Hong Kong dollar claims against banks abroad, at \$122.6 billion at end-August 2003, much larger than the level of \$24.4 billion at end-2002.

4.14 On the external position vis-à-vis banks in the Mainland, Hong Kong dollar liabilities owed by Hong Kong's authorized institutions to banks in the Mainland continued to be prominent, accounting for 36.4% of the total Hong Kong dollar liabilities to banks abroad at end-August 2003. Hong Kong dollar claims held by Hong Kong's authorized institutions on banks in the Mainland had a much smaller share, at 9.4% of the total Hong Kong dollar claims on banks abroad at end-August 2003. Owing to reduced deposits from banks in the Mainland, Hong Kong dollar liabilities owed by Hong Kong's authorized institutions to banks in the Mainland fell markedly, by 37.7% over end-2002 to \$45.9 billion at end-August 2003. On a year-on-year comparison, the decrease was even larger, by 41.0% at end-August 2003. On the other hand, with increased lending and placement to banks in the Mainland, Hong Kong dollar claims held by Hong Kong's authorized institutions on banks in the Mainland rose by 12.9% over end-2002 to \$23.3 billion at end-August 2003. On a year-on-year comparison, there was a surge of 16.3% at end-August 2003. As to the net position, Hong Kong's authorized institutions had net Hong Kong dollar liabilities to banks in the Mainland, amounting to \$22.6 billion at end-August 2003, considerably less than the level of \$52.9 billion at end-2002.

/Table 4.8

Table 4.8

**Hong Kong dollar external claims and liabilities
held by Hong Kong's authorized institutions**

<u>As at the end of</u>		<u>Claims on banks outside Hong Kong (HK\$Bn)</u>				<u>Liabilities to banks outside Hong Kong (HK\$Bn)</u>				<u>Net liabilities to banks outside Hong Kong (HK\$Bn)</u>	
		<u>Overall</u>		<u>Involving banks in the Mainland</u>		<u>Overall</u>		<u>Involving banks in the Mainland</u>		<u>Overall</u>	<u>Involving banks in the Mainland</u>
2002	Q1	171.8	(1.1)	19.1	(3.2)	147.0	(-16.2)	68.4	(-28.7)	-24.9	49.3
	Q2	190.1	(10.6)	19.8	(3.4)	151.2	(2.9)	67.4	(-1.4)	-38.9	47.6
	Q3	192.3	(1.2)	21.5	(8.7)	154.3	(2.1)	70.6	(4.6)	-38.0	49.0
	Q4	185.6	(-3.5)	20.6	(-4.2)	161.2	(4.5)	73.6	(4.3)	-24.4	52.9
2003	Q1	202.4	(9.0)	21.9	(6.4)	149.8	(-7.1)	62.2	(-15.4)	-52.5	40.3
	Q2	228.4	(12.9)	23.0	(4.6)	140.3	(-6.3)	54.9	(-11.7)	-88.6	32.0
	Jul	252.9	(10.7)	22.8	(-0.7)	128.8	(-8.2)	51.0	(-7.1)	-124.1	28.2
	Aug	248.8	(-1.6)	23.3	(2.2)	126.2	(-2.0)	45.9	(-10.1)	-122.6	22.6
		<32.4>		<16.3>		<-22.7>		<-41.0>			

Notes : () % change during the period.

< > % change over a year earlier.

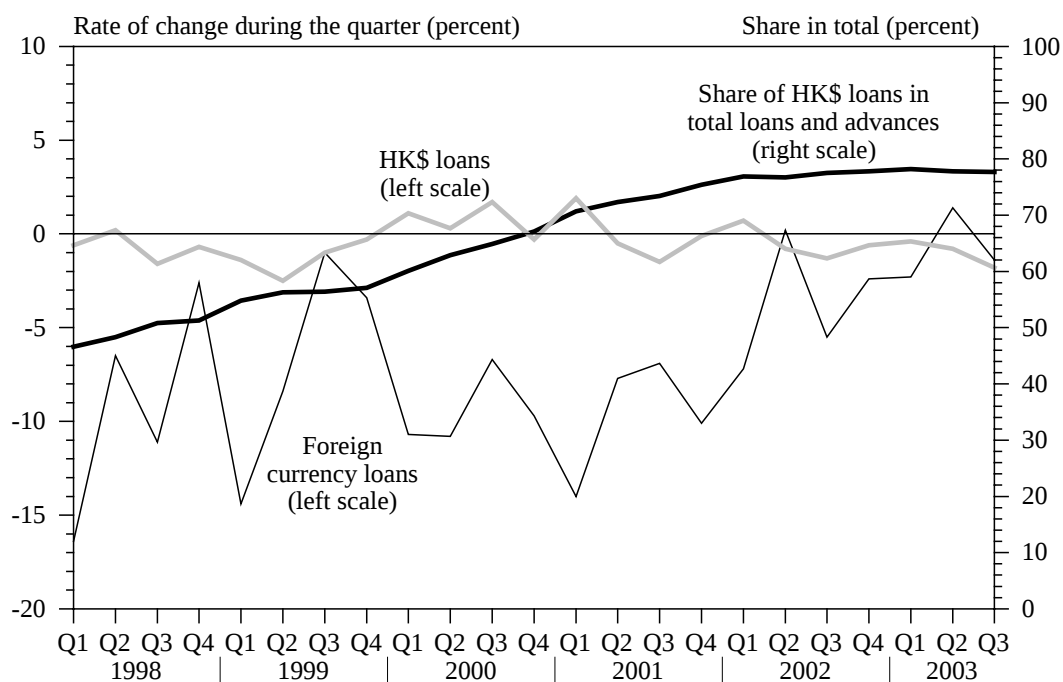
Loans and advances

4.15 Total loans and advances shrank by 1.7% during the third quarter of 2003 to \$2,018 billion at end-September, further to a 0.3% decline during the second quarter. Both Hong Kong dollar loans and foreign currency loans decreased during the third quarter, by 1.8% and 1.4% respectively to \$1,568 billion and \$450 billion at end-September. Yet at 77.7% and 22.3% at end-September, their shares in total loans and advances were little changed from those at end-June. On a year-on-year comparison, these two broad types of loans fell by 3.6% and 4.7% respectively at end-September 2003, giving a decrease in total loans and advances by 3.8%.

/Table 4.9

Table 4.9**Loans and advances by currency denomination**

% change during the quarter		Hong Kong dollar loans	Foreign currency loans	Total loans and advances
2002	Q1	0.7	-7.2	-1.2
	Q2	-0.8	0.2	-0.5
	Q3	-1.3	-5.5	-2.2
	Q4	-0.6	-2.4	-1.0
2003	Q1	-0.4	-2.3	-0.8
	Q2	-0.8	1.4	-0.3
	Q3	-1.8	-1.4	-1.7
Total amount at the end of September 2003 (HK\$Bn)		1,568	450	2,018
% change over a year earlier		-3.6	-4.7	-3.8

Diagram 4.6**Loans and advances by currency denomination and share of Hong Kong dollar loans in total loans and advances**

/4.16

4.16 As Hong Kong dollar loans contracted further while Hong Kong dollar deposits expanded further during the third quarter of 2003, the Hong Kong dollar loan-to-deposit ratio moved down appreciably further, to 83.2% at end-September, from 86.7% at end-June.

Table 4.10

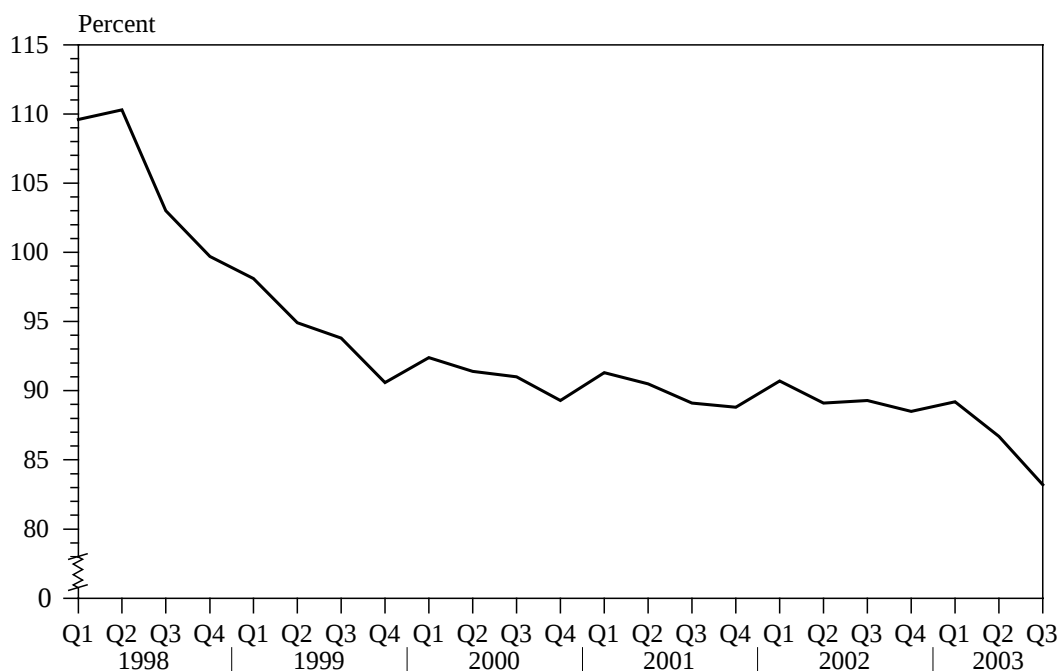
Hong Kong dollar loan-to-deposit ratio^(a)

<u>As at the end of</u>	<u>%</u>
2002 Q1	90.7
Q2	89.1
Q3	89.3
Q4	88.5
2003 Q1	89.2
Q2	86.7
Q3	83.2

Note : (a) Hong Kong dollar deposits have been adjusted to include foreign currency swap deposits.

Diagram 4.7

Hong Kong dollar loan-to-deposit ratio*



Note : (*) See the footnote to Table 4.10.

4.17 Analysed by place of usage, loans for use in Hong Kong dwindled by 1.7% during the third quarter of 2003 to \$1,788 billion at end-September, following a 0.3% reduction during the second quarter. Loans for use outside Hong Kong had a similar decrease, by 1.6% during the third quarter of 2003 to \$230 billion at end-September, after a 0.2% drop during the second quarter. But on a year-on-year comparison, loans for use outside Hong Kong fell to a much larger extent than loans for use in Hong Kong, by 10.2% as against 2.9% at end-September 2003, attributable in part to continued cut-back in Euro-yen Impact Loans⁽⁷⁾.

Table 4.11

Loans and advances by place of usage

% change during the quarter		Loans for use in Hong Kong ^(a)	Loans for use outside Hong Kong ^(b)
2002	Q1	0.1	-9.6
	Q2	-0.5	-0.8
	Q3	-1.6	-6.6
	Q4	-0.4	-5.4
2003	Q1	-0.5	-3.4
	Q2	-0.3	-0.2
	Q3	-1.7	-1.6
Total amount at the end of September 2003 (HK\$Bn)		1,788	230
% change over a year earlier		-2.9	-10.2

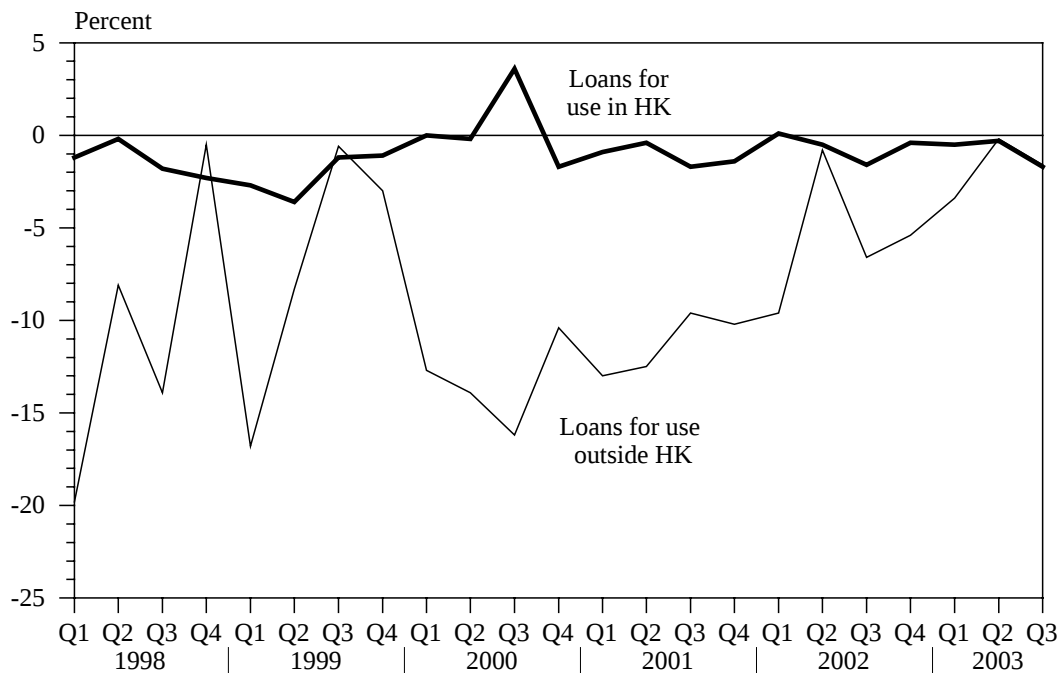
Notes : (a) Including trade financing loans.

(b) Including loans where the place of usage is unknown.

/Diagram 4.8

Diagram 4.8

**Loans and advances by place of usage
(rate of change during the quarter)**



4.18 Analysed by major usage, domestic loans continued to show mixed developments. Specifically, loans to stockbrokers bounced up by 10.0% during the third quarter of 2003, reversing the 5.5% decline during the second quarter. This was partly attributable to an upsurge in stock market activity in the more recent months. Loans to financial concerns and to the manufacturing sector went up further, by 3.7% and 3.1% respectively during the third quarter, having increased by 2.8% and 4.9% during the second quarter. On the other hand, loans to the wholesale and retail trades declined by 5.4% during the third quarter, further to a 0.5% drop during the second quarter. Loans for building, construction, property development and property investment, and for purchase of residential property also shrank further, by 2.2% and 1.0% respectively during the third quarter, following decreases of 1.3% and 1.4% during the second quarter. Trade financing loans fell back, by 1.4% during the third quarter, after a 6.2% rise during the second quarter.

/Table 4.12

Table 4.12**Loans and advances for use in Hong Kong by major usage^(a)**

		Loans to :							
% change during the quarter		Finance visible trade	Manu- facturing sector	Whole- sale and retail trades	Building, construction, property develop- ment and property investment	Purchase resi- dential property ^(b)	Financial concerns	Stock- brokers	Others
2002	Q1	-2.6	1.2	1.0	-0.5	*	0.9	2.1	0.7
	Q2	7.3	1.3	-0.1	-1.9	0.6	-8.2	23.9	-0.8
	Q3	1.9	-4.9	-0.9	-2.4	-0.7	-3.2	-22.2	-1.5
	Q4	-3.7	1.2	-2.6	1.0	-0.7	0.3	-5.3	-0.3
2003	Q1	2.2	1.7	2.3	-0.3	-1.3	0.1	4.2	-1.2
	Q2	6.2	4.9	-0.5	-1.3	-1.4	2.8	-5.5	-0.9
	Q3	-1.4	3.1	-5.4	-2.2	-1.0	3.7	10.0	-4.4
Total amount at the end of September 2003 (HK\$Bn)		97	78	97	365	618	134	9	391
% change over a year earlier		3.1	11.3	-6.2	-2.8	-4.4	7.0	2.6	-6.7

Notes : (a) Figures in this table are revised on a regular basis to incorporate subsequent amendments and loan re-classifications made by the authorized institutions concerned. The rates of change for the earlier quarters have been adjusted for the revisions known up to the latest reference quarter.

(b) Including loans for the purchase of flats under the Home Ownership Scheme, Private Sector Participation Scheme, and Tenants Purchase Scheme.

(*) Change of less than 0.05%.

4.19 The quality of assets held by the local banking sector, having undergone some deterioration in the first quarter of 2003, improved appreciably in the latter part of the second quarter, in tandem with the revival in business activity. Reflecting this, the ratio of non-performing loans to total loans came down, from 4.03% at end-March to 3.83% at end-June, as did the ratio of overdue and rescheduled loans to total loans, from 3.64% to 3.61%⁽⁸⁾. The ratio of classified loans to total loans also declined, from 5.03% to 4.76% over the same period. Amongst the various types of loans, arrears for over three months in mortgage repayment went up only marginally, from 1.11% at end-March to 1.12% at end-June, while arrears for over three months in credit card repayment also rose slightly, from 1.25% to 1.27%. In overall terms, the local banks remained well capitalised, with their consolidated capital adequacy ratio averaging at 15.6% at end-June 2003, way above the standard set by the Bank for International Settlements.

/Banks

Banks and other deposit-taking institutions

4.20 During the third quarter of 2003, the number of licensed banks decreased by two to 134 at end-September. Concurrently, the number of restricted licence banks fell by one to 41, while the number of deposit-taking companies remained unchanged at 40. Altogether, 215 authorized institutions (excluding representative offices) from 33 countries and territories had a presence in Hong Kong at end-September. Taking all the authorized institutions in Hong Kong together, their total assets went up by 2.0% during the third quarter of 2003 to \$6,170 billion at end-September.

4.21 On enhancing deposit protection in Hong Kong, opinions obtained from an earlier public consultation by HKMA indicated broad support for introduction of a deposit protection scheme in Hong Kong. After further studies and another round of public consultation by HKMA on the details of the proposed scheme, the bill for establishing the deposit protection scheme in Hong Kong was drawn up and introduced into the Legislative Council on 30 April 2003. In order to prevent moral hazard and ensure financial viability of the scheme, it is proposed that the amount of protection for each eligible claim be capped at a specified level, and that a system of differential contributions from the depository institutions according to their regulatory ratings be introduced. It is expected to take at least 18 months after the passage of the bill for the scheme to commence operation.

/4.22

4.22 To help address the issue of increases in consumer credit defaults and personal bankruptcies, the revised Code of Practice on Consumer Credit Data has become effective as from 2 June 2003. Designed to provide practical guidance to data users in the handling of consumer credit data, the revised Code of Practice covers the collection, accuracy, use, security, access and correction aspects, as they relate to the personal data of those individuals who are or have been applicants for consumer credit. It covers, on the one hand, credit reference agencies, and on the other hand, credit providers in their dealing with credit reference agencies and debt collection agencies.

4.23 As another initiative to facilitate credit assessment and maintain soundness of the local banking sector, HKMA, the Hong Kong Association of Banks and the Deposit Taking Companies Association jointly announced on 16 June 2003 a plan to establish a commercial credit reference agency (CCRA) in Hong Kong in the third quarter of 2004. CCRA is expected to collect credit data of small and medium-sized enterprises and make such data available to the authorized institutions. To safeguard confidentiality of the data held by CCRA, HKMA will issue a supervisory guideline to set out the minimum standards that authorized institutions have to observe in respect of sharing and use of the commercial credit data. The draft guideline is currently under consultation.

Insurance

4.24 At end-September 2003, there were 190 insurance companies in Hong Kong, same as at end-June. Within this total, 46 were engaged in long-term or life insurance business, 125 in general business, and 19 in composite business. Taken together, insurance companies from 25 countries and territories maintained a presence in Hong Kong at end-September. Underpinned by robust expansion in life insurance, the value of business receipts in the insurance industry surged by 14.4% in the second quarter of 2003 over a year earlier, following a 22.4% leap in the first quarter.

/The

The debt market

4.25 In the third quarter of 2003, a total of 29 issues of Exchange Fund paper were launched by HKMA to replace those outstanding issues approaching maturity⁽⁹⁾. The total market value of Exchange Fund paper outstanding rose by 0.6% during the third quarter of 2003 to \$119.7 billion at end-September. Market response to the tenders of Exchange Fund paper remained favourable, with an average over-subscription rate of 6.0 times in the third quarter, albeit slightly less than that of 6.3 times in the second quarter. Trading in Exchange Fund paper continued to be active, with the daily turnover averaging at \$16.7 billion in the third quarter of 2003, though also smaller than that of \$23.8 billion in the second quarter. Comparing end-September 2003 with end-June 2003, the yield spread of five-year Exchange Fund Notes over the corresponding US Treasuries narrowed from 28 basis points to 24 basis points.

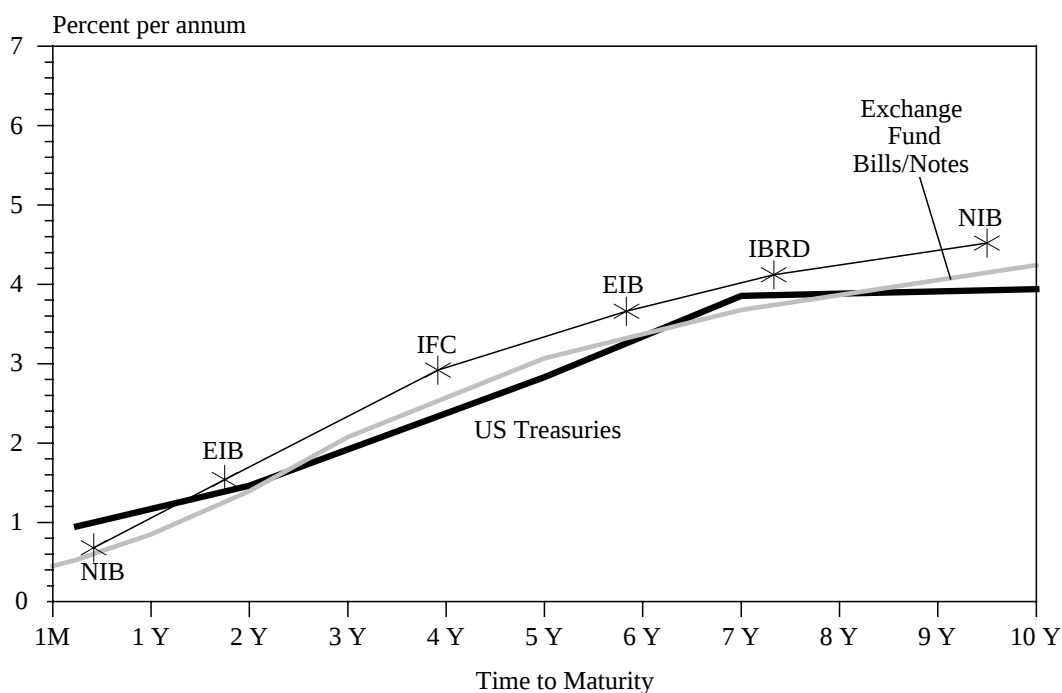
Table 4.13

Exchange Fund Bills and Notes issued by HKMA

		Amount outstanding as at the end of the quarter (HK\$Bn)	Average daily turnover in the quarter (HK\$Bn)
2002	Q1	114.7	22.3
	Q2	115.7	22.7
	Q3	116.6	23.4
	Q4	117.5	21.0
2003	Q1	118.2	27.8
	Q2	119.0	23.8
	Q3	119.7	16.7

/Diagram 4.9

Diagram 4.9
Hong Kong dollar and US dollar yield curves
(as at the end of September 2003)



Note : AAA Hong Kong dollar debt issuers

EIB	European Investment Bank
IBRD	International Bank for Reconstruction and Development
IFC	International Finance Corporation
NIB	Nordic Investment Bank

4.26 At present, the Hong Kong Mortgage Corporation (HKMC) is one of the major issuers of debt securities in Hong Kong. In the third quarter of 2003, \$4.0 billion worth of HKMC debt paper was launched. At end-September, the total outstanding value of debt securities issued by HKMC under its Note Issuance Programme amounted to \$4.5 billion, and that under its Debt Issuance Programme reached \$25.8 billion. In addition, retail bonds were issued by HKMC, with the outstanding value totalling \$5.4 billion at end-September.

/4.27

4.27 In the third quarter of 2003, \$21.3 billion worth of negotiable certificates of deposit (NCDs) was launched, less than that of \$29.3 billion issued in the second quarter. Of the new issuance of NCDs in the third quarter, \$13.8 billion was denominated in Hong Kong dollars, also down from that of \$17.3 billion in the second quarter. The total value of NCDs outstanding fell slightly to \$232.8 billion at end-September, from \$234.7 billion at end-June. Within the total at end-September, \$130.1 billion was denominated in Hong Kong dollars, smaller than that of \$139.5 billion at end-June. Notwithstanding this, the proportion of Hong Kong dollar denominated NCDs held by the local banking sector rose, to 51.3% at end-September, from 50.6% at end-June.

Table 4.14

NCDs issued by authorized institutions in Hong Kong

		<u>Issued and outstanding</u> (HK\$Bn)		<u>Held by authorized institutions</u> (HK\$Bn)		<u>Held outside the local banking sector</u> (HK\$Bn)	
<u>As at the end of</u>		<u>In HK\$</u>	<u>Total</u>	<u>In HK\$</u>	<u>Total</u>	<u>In HK\$</u>	<u>Total</u>
2002	Q1	132.1	173.3	73.5	85.0	58.6	88.2
	Q2	142.0	192.3	77.2	86.2	64.8	106.1
	Q3	136.8	201.0	72.9	82.0	63.9	118.9
	Q4	138.4	211.2	72.4	80.2	66.1	131.1
2003	Q1	140.6	229.5	74.0	83.1	66.6	146.4
	Q2	139.5	234.7	70.6	79.2	69.0	155.5
	Q3	130.1	232.8	66.7	76.7	63.4	156.1

/4.28

4.28 In the third quarter of 2003, 188 new issues of other Hong Kong dollar debt instruments, worth \$24.9 billion, were launched by the private sector. Partly reflecting risk aversion by debt issuers against potential interest rate volatility, the issuance of fixed rate bonds by the private sector, at \$18.7 billion in the third quarter of 2003, continued to exceed considerably that of floating rate notes, at \$6.2 billion in the same quarter. At end-September 2003, the total outstanding value of Hong Kong dollar fixed rate bonds and floating rate notes issued by the private sector amounted to \$212.7 billion and \$87.1 billion respectively, adding up to a total of \$299.8 billion⁽¹⁰⁾. These exceeded the corresponding figures of \$206.1 billion, \$85.0 billion and \$291.1 billion at end-June 2003. Furthermore, there were four new issues of Hong Kong dollar debt paper by multilateral agencies in the third quarter of 2003, raising a total of \$0.9 billion, as against nil issue in the second quarter.

4.29 Taking the public and private sectors together, the total value of Hong Kong dollar debt paper outstanding thus amounted to \$555.9 billion at end-September 2003⁽¹¹⁾, up from \$552.9 billion at end-June 2003. The size of the Hong Kong dollar debt market was equivalent to 26.8% of HK\$M3, or 20.4% of the Hong Kong dollar denominated assets of the entire banking sector.

The stock, futures and gold markets

4.30 The local stock market, having shown a distinct upturn since late April, rose significantly further during the third quarter of 2003. It was underpinned by growing optimism about the performance and near-term outlook of the Hong Kong economy. Further lifting market sentiment were signing of CEPA, implementation of the “individual visit” scheme for Mainland visitors to Hong Kong, and a rebound in activity in the residential property market. Increased inflow of funds into the region gave an additional boost. The general uptrend in the overseas stock markets also contributed. As a result, the Hang Seng Index surged amidst active market trading, reaching a high at 11 296 on 24 September. While profit-taking in the latter part of the month pared some of the earlier gains, the Hang Seng Index managed to close at 11 230 at the end of September, 17.3% higher than the level at end-June, and 33.5% higher than the trough at 8 409 on 25 April. (The Hang Seng Index rose further, to a new high at 12 251 on 21 October, upon further inflow of funds and probably also in the light of the Government’s announcement of additional measures to stabilise the residential property market. It broadly hovered within 11 700 - 12 400 thereafter, with a leap to another new high at 12 441 on 4 November, before settling back to close at 11 845 on 20 November.)

/Diagram 4.10

Diagram 4.10

Hang Seng Index



/Table 4.15

Table 4.15

**Movements in the Hang Seng Index and
in the share price indices in selected stock markets overseas
(index as at the last trading day of the quarter)**

		Hang Seng <u>Index</u>	New York Dow Jones Industrial <u>Average</u>	Tokyo Nikkei <u>Average</u>	London FTSE 100 <u>Index</u>	Frankfurt DAX 30 <u>Index</u>	Paris CAC 40 <u>Index</u>	Sydney All Ordinaries <u>Index</u>	Singapore Straits Times <u>Index</u>
2002	Q1	11 033	10 404	11 025	5 272	5 397	4 688	3 363	1 803
	Q2	10 599	9 243	10 622	4 656	4 383	3 898	3 163	1 553
	Q3	9 072	7 592	9 383	3 722	2 769	2 777	2 928	1 352
	Q4	9 321	8 342	8 579	3 940	2 893	3 064	2 976	1 341
2003	Q1	8 634	7 992	7 973	3 613	2 424	2 618	2 849	1 268
	Q2	9 577	8 985	9 083	4 031	3 221	3 084	3 000	1 448
	Q3	11 230	9 275	10 219	4 091	3 257	3 135	3 176	1 631
% increase during the third quarter of 2003		17.3	3.2	12.5	1.5	1.1	1.7	5.9	12.6
% increase during the first nine months of 2003		20.5	11.2	19.1	3.8	12.6	2.3	6.7	21.6
% increase at end-September 2003 over a year earlier		23.8	22.2	8.9	9.9	17.6	12.9	8.5	20.6

/Box 4.2

Box 4.2

Recent movements in the Hang Seng Sectoral Sub-indices

Same as the overall Hang Seng Index, the Hang Seng Sectoral Sub-indices all went higher during the third quarter of 2003. Yet the increases showed considerable variations in magnitude.

Hang Seng Index and its Sectoral Sub-indices

	<u>Index level as at end-2002</u>	<u>Index level as at end-Jun 2003</u>	<u>Index level as at end-Sep 2003</u>	<u>% increase between end-2002 and end-Sep 2003</u>	<u>% increase between end-Jun and end-Sep 2003</u>
Hang Seng Index	9 321	9 577	11 230	20.5	17.3
Sub-indices :					
Finance	18 231	19 420	22 342	22.5	15.0
Commerce and Industry	4 044	4 135	4 820	19.2	16.6
Properties	11 104	10 225	14 383	29.5	40.7
Utilities	21 971	22 803	22 944	4.4	0.6

The Properties Sub-index had the strongest surge, by 40.7% between end-June and end-September 2003. While improved performance and near-term outlook of the Hong Kong economy and increased inflow of funds were the main background factors boosting overall sentiment, the visible rebound in the property market more recently generated much investment interest in property-related shares. Expectation for additional measures to support the property market prior to the Government's announcement in October added to the enthusiasm. The Commerce and Industry Sub-index and the Finance Sub-index also leaped, though less sharply, by 16.6% and 15.0% respectively, attributable to revival in overall business activity and announcement of some favourable corporate results. By comparison, the Utilities Sub-index had just a slight rise, by 0.6%, as public utilities shares, characterised by steady corporate earnings and dividend yields, used to be in relatively lesser demand during an economic upswing than during an economic downturn.

A broadly similar profile was observed for the first nine months of 2003. Comparing end-September 2003 with end-2002, the Properties Sub-index went up most notably, by 29.5%. The Finance Sub-index and the Commerce and Industry Sub-index had relatively smaller, yet still significant, increases, by 22.5% and 19.2% respectively. The Utilities Sub-index fared much less well, rising by only 4.4%.

As at end-September 2003, the Finance Sub-index maintained the largest weighting in the Hang Seng Index, at 42.5%. This was followed by the Commerce and Industry Sub-index (with a weighting of 39.4%), the Properties Sub-index (12.2%), and the Utilities Sub-index (6.0%).

/4.31

4.31 Mainly consequential to the leap in share prices, total stock market capitalisation, including the Main Board and the Growth Enterprise Market (GEM)⁽¹²⁾, soared by 20.4% during the third quarter of 2003 to \$4,776 billion at end-September. Concurrently, the average daily turnover leaped to \$12.0 billion in the third quarter of 2003, from \$8.1 billion in the second quarter.

Table 4.16

**Average daily turnover and total market capitalisation
of the Hong Kong stock market**

		<u>Average daily turnover in the quarter (HK\$Bn)</u>			<u>Total market capitalisation as at the end of the quarter (HK\$Bn)</u>		
		<u>Main Board</u>	<u>Growth Enterprise Market</u>	<u>Total</u>	<u>Main Board</u>	<u>Growth Enterprise Market</u>	<u>Total</u>
2002	Q1	6.9	0.3	7.1	3,855	69	3,924
	Q2	7.8	0.2	8.0	3,792	61	3,852
	Q3	5.8	0.2	5.9	3,327	53	3,381
	Q4	5.6	0.1	5.6	3,559	52	3,611
2003	Q1	6.0	0.1	6.1	3,378	51	3,429
	Q2	7.9	0.1	8.1	3,907	61	3,968
	Q3	11.8	0.2	12.0	4,708	68	4,776

4.32 In the third quarter of 2003, 21 new share flotations were launched on the Stock Exchange of Hong Kong, raising a total equity capital of \$7.8 billion. Of these, 15 were listed on the Main Board and six on GEM, raising equity capital of \$7.6 billion and \$0.2 billion respectively. Amongst the new issues, two pertained to H shares, with one listed on the Main Board and the other on GEM, raising equity capital of \$2.4 billion and \$0.06 billion respectively. Separately, \$4.5 billion was raised through private placements by 24 companies, and \$0.8 billion through rights issues by 12 companies.

/4.33

4.33 As to trading in derivatives on the market at the Hong Kong Exchanges and Clearing Limited, the average daily turnover of Hang Seng Index futures contracts rose by 11.5% over the second quarter of 2003 to 30 281 contracts in the third quarter, whereas the average daily turnover of Hang Seng Index options contracts fell by 2.3% to 9 524 contracts. On MSCI China Free Index futures contracts⁽¹³⁾, trading remained scant, with an average daily turnover of only one contract in both the second and third quarters of 2003.

Table 4.17

**Average daily turnover of Hang Seng Index futures
and options contracts in the Hong Kong derivatives market**

<u>During the quarter</u>		<u>Hang Seng Index futures contracts</u> (no. of contracts)	<u>Hang Seng Index options contracts</u> (no. of contracts)
2002	Q1	17 956	3 338
	Q2	18 739	3 185
	Q3	21 053	4 652
	Q4	20 508	6 242
2003	Q1	22 408	8 633
	Q2	27 152	9 746
	Q3	30 281	9 524

4.34 At end-September 2003, there were 34 classes of stock options contracts. The average daily turnover, at 16 313 contracts in the third quarter of 2003, was up by 22.1% from the second quarter. As regards stock futures contracts, while there were also 34 classes at end-September 2003, the average daily turnover increased more sharply from a much thinner base, by 49.2% from the second quarter to 91 contracts in the third quarter.

4.35 Comparing the third quarter with the second quarter of 2003, the average daily turnover of three-month HIBOR futures contracts dropped by 47.6% to 97 contracts, and the average daily turnover of three-year Exchange Fund Note futures contracts by seven contracts to just one contract.

4.36 At end-September 2003, 415 issues of warrants were listed on the Main Board, comprising 46 issues of equity warrants and 369 issues of derivative warrants. The average daily turnover of equity warrants rose substantially, to \$8.9 million in the third quarter of 2003, six times more than the level in the second quarter. The average daily turnover of derivative warrants also surged, by 52.6% from the second quarter to \$1.1 billion in the third quarter. Yet on GEM, there were only two issues of warrants listed at end-September 2003. Trading in them remained thin in the third quarter.

4.37 Gold price resumed an uptrend in the third quarter of 2003, after undergoing some consolidation in the second quarter. The increase was more distinct in the latter part of the third quarter, with the price of loco-London gold reaching a seven-year high of US\$391.3 per troy ounce on 25 September. Besides a weaker US dollar, the upsurge was triggered by OPEC's decision to cut its oil production and by heightened political tension in the Middle East. Growing speculation that the European Central Bank would exercise restraint in reducing its gold reserves upon expiry of its present agreement in September 2004 also contributed. Although profit-taking brought the price down to US\$383.7 per troy ounce at end-September, it was still 11.2% up from US\$345.2 per troy ounce at end-June. Gold price at the Chinese Gold and Silver Exchange Society exhibited a similar profile, surging in most of the third quarter to \$3,534 per tael at end-September, up by 10.3% from \$3,204 per tael at end-June. Turnover on the Exchange amounted to 0.81 million taels in the third quarter of 2003, considerably higher than that of 0.66 million taels in the second quarter.

/Unit

Unit trusts and mutual funds

4.38 At end-September 2003, the total number of unit trusts and mutual funds (including sub-funds and umbrella funds) in Hong Kong was 972, down from 986 at end-June. Gross sales of mutual funds amounted to US\$5.0 billion in the third quarter of 2003, up by 7.1% over the second quarter. Net sales after deducting redemptions rose by 27.8% from the second quarter to US\$0.8 billion in the third quarter. Amongst the various types of mutual funds, equity funds continued to account for the largest share, at 58.0% of the total value of funds at end-September. This was followed by bond funds, asset allocation funds and money market funds, with respective shares of 27.5%, 7.9% and 6.0%⁽¹⁴⁾.

4.39 The Mandatory Provident Fund (MPF) System⁽¹⁵⁾ continues to generate a substantial amount of retirement fund assets which, in the course of time, should support further development of the local capital market. The aggregate net asset value of the approved constituent funds of MPF schemes rose further to \$78.7 billion at end-September 2003, from \$69.2 billion at end-June. This was mainly attributable to continued contributions from the enrolled population. By end-September, there were 19 approved corporate trustees. On MPF products, 44 master trust schemes, two industry schemes and two employer sponsored schemes, comprising altogether 319 constituent funds, were approved by the Mandatory Provident Fund Schemes Authority. About 216 000 employers, 1.74 million employees and 300 000 self-employed persons had been enrolled in MPF schemes, with the compliance rates for employers, relevant employees and self-employed persons reaching 94.9%, 95.7% and 85.4% respectively.

/Notes

Notes :

- (1) Under the linked exchange rate system established in October 1983, the note-issuing commercial banks are required to pay US dollars to the Hong Kong Monetary Authority (HKMA) for the account of the Exchange Fund at the fixed rate of HK\$7.8 to US\$1.0 in return for non-interest-bearing Certificates of Indebtedness (CIs), as backing for the issue of their Hong Kong dollar banknotes. As from 7 September 1998, HKMA also provides an explicit undertaking to convert the Hong Kong dollar balances held in the clearing accounts maintained by the banks with HKMA at the Convertibility Undertaking Rate. This was set at the then market exchange rate of 7.750 when the convertibility undertaking was introduced. From 1 April 1999, the Convertibility Undertaking Rate for the Aggregate Balance was raised from 7.750 by 1 pip per calendar day, reaching 7.800 on 12 August 2000, where it has stayed.
- (2) The trade-weighted Nominal Effective Exchange Rate Index (EERI) is an indicator of the overall exchange value of the Hong Kong dollar against a fixed basket of other currencies. These currencies are selected on account of their importance in Hong Kong's trade, and the weights reflect their relative importance in Hong Kong's merchandise trade.

As from 2 January 2002, a new series of nominal Effective Exchange Rate Index replaces the old series. The weights adopted for the new EERI series are based on the average pattern of Hong Kong's merchandise trade during 1999 and 2000, as against that during 1991 to 1993 for the old series. The currency basket for the new series has also been updated to include the euro and the Philippine peso, and to exclude the five currencies pertaining to the participating countries of the euro. Thus the currency basket for the new series contains 14 currencies, instead of 17 currencies for the old series. The base period is changed from October 1983 to January 2000.

The corresponding Real EERI, which takes into account the relative movements in the seasonally adjusted consumer price indices of the respective economies, is revised accordingly, in line with the updated weights and the new base period of the nominal EERI.

It is important to note that the EERIs thus compiled adopt constant weights on the respective currencies, while the pattern of merchandise trade changes over time. In particular, Hong Kong's trade with the Mainland has shifted more towards re-exports, from domestic exports and retained imports. Also, with the Mainland being the largest source of Hong Kong's re-exports, movements in the exchange rate of the renminbi could have somewhat different implications for Hong Kong's export competitiveness, as against movements in the other currencies.

/(3)

- (3) In the light of the changing market shares of individual authorized institutions (AIs) in the residential mortgage business, the coverage of the Monthly Survey on Residential Mortgage Lending conducted by HKMA has been expanded as from May 2001, in order to increase the proportion of business covered by the survey. Altogether 38 AIs were so included immediately after the coverage expansion. The number of AIs has since fallen to 28 due to banking sector consolidation. The AIs currently covered together account for around 96% of the total business, as compared to 92% for the 32 AIs formerly covered. The outstanding amount of mortgage loans covered by the survey is hence lifted, by 8.8%.
- (4) Foreign currency swap deposits are deposits involving customers buying foreign currencies in the spot market and placing them as deposits with authorized institutions, whilst at the same time entering into a contract to sell such foreign currencies (principal plus interest) forward in line with the maturity of such deposits. For most analytical purposes, they should be regarded as Hong Kong dollar deposits.
- (5) The various definitions of the money supply are as follows:
- M1 : notes and coins with the public, plus customers' demand deposits with licensed banks.
- M2 : M1 plus customers' savings and time deposits with licensed banks, plus negotiable certificates of deposit (NCDs) issued by licensed banks and held outside the monetary sector.
- As from June 2002, short-term Exchange Fund placements of less than one month are included under time deposits as part of the monetary aggregates. The data series on time deposits and M2 are backdated to April 1997 using this revised definition.
- M3 : M2 plus customers' deposits with restricted licence banks and deposit-taking companies, plus NCDs issued by such institutions and held outside the monetary sector.
- (6) Amongst the various monetary aggregates, more apparent seasonal patterns are found in HK\$M1, currency held by the public, and demand deposits. Seasonally adjusted data on these three series back-dated to January 1990 have been compiled. The deseasonalised data facilitate analysis of the underlying trends. For details, see the November 2000 issue of the HKMA Quarterly Bulletin.
- (7) Euro-yen Impact Loans (EYIL) are loans made to customers in Japan by a domestic branch of a Japanese bank but booked in an overseas branch of the bank. Loans booked in this way generally have tax and funding cost advantages for customers. Reflecting a more cautious lending stance by the Japanese banks and the need to reduce the size of their balance sheets, EYIL has declined substantially since the second half of 1997.

- (8) Overdue loans are defined here as those that have been overdue for more than three months. Rescheduled loans are those that have been restructured or renegotiated because of deterioration in the financial position of the borrower, or because of inability of the borrower to meet the original repayment schedule. Non-performing loans are those on which interest has been placed in suspense or on which interest accrual has ceased. Classified loans are those that have been classified as substandard, doubtful or loss. Of these categorisations, classified loans overlap to a certain extent with overdue and rescheduled loans.
- (9) As from 1 April 1999, interest payments on Exchange Fund paper are allowed for expanding the stock of outstanding Exchange Fund paper.
- (10) These figures may not represent a full coverage of all the Hong Kong dollar debt paper issued by the private sector.
- (11) Due to different sources for NCD data, the total value of Hong Kong dollar debt paper outstanding may not equal the sum of the outstanding values of Exchange Fund paper, HKMC debts, NCDs, and other Hong Kong dollar debt instruments issued by the private sector.
- (12) The Growth Enterprise Market was launched by the then Stock Exchange of Hong Kong Ltd in November 1999 as an alternative market to the Main Board, in order to give emerging growth companies easier access to the funds of the investing public. Though open to companies in all industries and of all sizes, the market provides an efficient venue for fund raising especially by small to medium-sized enterprises.
- (13) The MSCI China Free Index is a market-capitalisation-weighted stocks index, covering Red-chip shares and H shares listed in Hong Kong, B shares listed in Shanghai and Shenzhen, and N shares listed in New York. The Index thus represents the universe of Chinese stocks open to investors outside the Mainland, and complements the Red-chip and H share markets in Hong Kong. Trading in MSCI China Free Index futures contracts commenced on 7 May 2001.
- (14) These figures are sourced from the sales and redemptions and performance survey conducted by the Hong Kong Investment Funds Association on their members, and as such cover only the active authorized funds that have responded to the survey.

/(15)

- (15) The Mandatory Provident Fund (MPF) System, launched on 1 December 2000, is a privately managed mandatory system of provident fund schemes covering members of the workforce aged between 18 and 65, subject to certain exceptions. It provides for joint contributions by the employer and the employee, each at 5% of the employee's relevant income, to a registered MPF scheme, subject to a maximum and a minimum level of income for MPF contribution purposes. As from February 2003, the minimum income level for MPF contribution purpose is raised from \$4,000 per month to \$5,000, yet the maximum income level is kept at \$20,000 per month. The accrued MPF benefits are fully vested in the scheme, and members can be transferred from scheme to scheme when there is a change in employment.

The Mandatory Provident Fund Schemes Authority (MPFA) is the statutory body tasked with the responsibility for regulation and supervision of the MPF System and for ensuring compliance with the Mandatory Provident Fund Schemes Ordinance.

An MPF scheme may consist of one or more constituent funds each with its own investment policy. A constituent fund may maintain a portfolio of direct investment in equities, bonds or other debt instruments, or may invest in approved pooled investment funds which may be in the form of unit trusts authorized by the Securities and Futures Commission or insurance policies issued by authorized insurers. Both constituent funds and pooled investment funds have to be approved by MPFA, and be subject to investment standards applicable to MPF investment funds. Following a recent legislative amendment, a constituent fund may also invest in some other types of financial products, such as index-tracking collective investment schemes, subject to MPFA's prior approval.

CHAPTER 5 : THE LABOUR SECTOR

Overall labour market situation

5.1 Labour market conditions, having deteriorated markedly during the second quarter and the beginning of the third quarter under the severe impact of SARS, showed a visible improvement towards the end of the third quarter, as SARS had come under control and as overall economic activity staged a progressive upturn. The *seasonally adjusted unemployment rate*⁽¹⁾ fell back to 8.3% in the third quarter of 2003, following a leap from 7.5% in the first quarter to 8.6% in the second quarter and further to a historical high of 8.7% in May - July. The number of unemployed persons (not seasonally adjusted) likewise dropped, to 297 300 in the third quarter of 2003, after elevating from 259 800 in the first quarter to 300 000 in the second quarter and further to a peak of 309 400 in June - August. However, the median duration of unemployment lengthened from 82 days to 90 days between the second and third quarters of 2003, along with an increase in the proportion of persons unemployed for six months or more from 28% to 31%. (In August - October 2003, the seasonally adjusted unemployment rate had a further fall, to 8.0% (provisional).)

5.2 The *underemployment rate*⁽²⁾ concurrently declined, to 3.6% in the third quarter of 2003, after leaping from 2.9% in the first quarter to 4.3% in the second quarter. Conceivably, many of the affected employees, having earlier been suspended from work or asked to take no-pay leave, had returned to their jobs more recently. This was notably so for those workers engaged in the tourism and consumption-related sectors. The number of underemployed persons likewise decreased, to 126 600 in the third quarter of 2003, following a lift from 100 700 in the first quarter to 151 000 in the second quarter. (In August - October 2003, the underemployment rate went down further, to 3.5% (provisional).)

/5.3

5.3 For the employed workers, there was a notable shift towards greater work intensity in the more recent months. Reflecting this, the number of employed persons working for 35 hours or more per week went up by 3.1% between the second and third quarters of 2003, while the number of employed persons working for less than 35 hours per week went down by 22.8%. Moreover, the proportion of employed persons working for 50 hours or more per week increased, from 36% in the second quarter to 40% in the third quarter, as did the proportion of employed persons working for 60 hours or more per week, from 22% to 23%. Consequently, the median hours of work for the employed workforce rose from 45 hours per week to 48 hours per week between the two quarters.

Table 5.1

Unemployment and underemployment rates

		Seasonally adjusted <u>unemployment rate</u> (%)	<u>Underemployment rate</u> (%)
2002	Annual	7.3	3.0
	Q1	7.0	3.2
	Q2	7.7	2.9
	Q3	7.4	2.9
	Q4	7.2	3.1
2003	Q1	7.5	2.9
	Q2	8.6	4.3
	Q3	8.3	3.6
	May - Jul	8.7	4.2
	Jun - Aug	8.6	4.0
	Jul - Sep	8.3	3.6

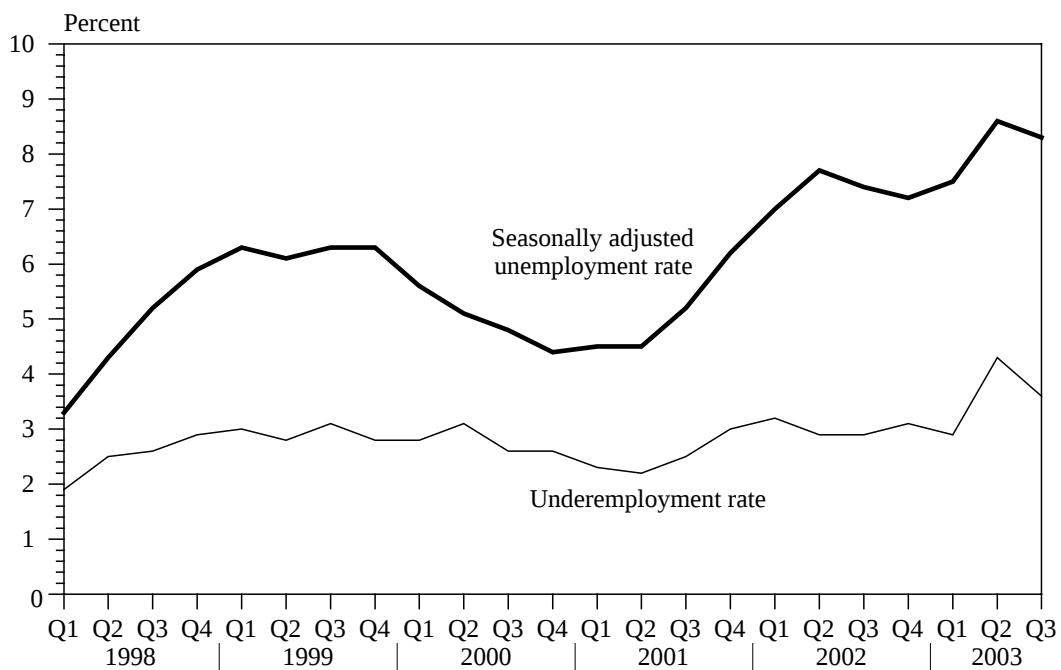
Note : Labour force statistics for 2002 have been slightly revised, upon finalisation of the end-2002 population estimates in August 2003. The revised statistics have been incorporated into Tables 5.1 - 5.16 and Diagrams 5.1 - 5.5 and 5.10.

Source : General Household Survey, Census and Statistics Department.

/Diagram 5.1

Diagram 5.1

Unemployment and underemployment rates



/Box 5.1

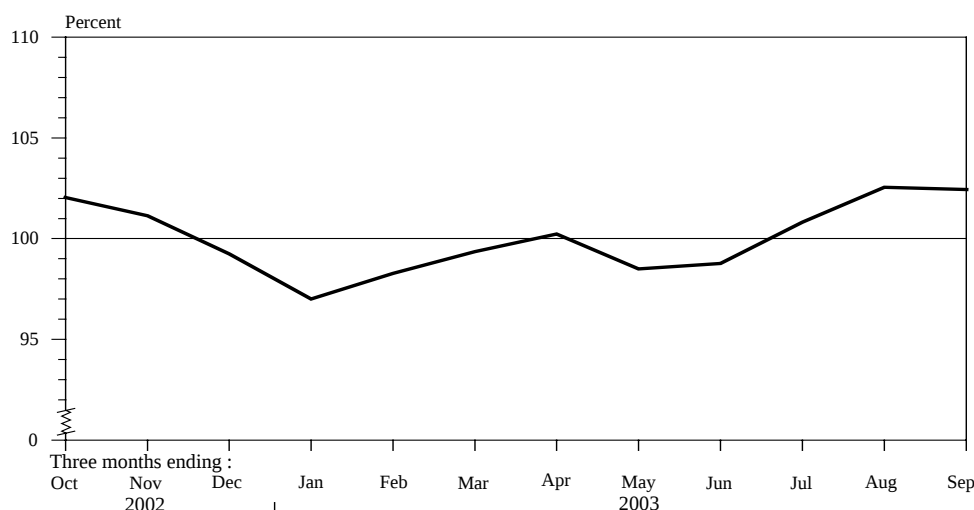
Box 5.1

Seasonal adjustment to the unemployment rate

Past data series shows that the unemployment figures tend to be influenced by seasonal variations over the course of a year, such as increased business activity and thus labour demand around the Christmas and Lunar New Year Holidays, relative slack in business activity and thus labour demand in the latter part of the first quarter, entry of a new batch of fresh graduates and school leavers into the labour force during the summer months, etc.

In order to make the underlying trend of the unemployment rate more discernible, the data series on unemployment rate is seasonally adjusted using the widely adopted X-11 ARIMA method to remove the effect of seasonal variations. Application of this method to the Hong Kong data basically involves first, the derivation of seasonal factors for adjusting the employment and unemployment figures, based on the respective data series over the past five complete years. Then, the seasonally adjusted employment and unemployment figures are added together to give the seasonally adjusted labour force. Finally, the seasonally adjusted unemployment rate is derived by dividing the seasonally adjusted number of unemployed persons by the seasonally adjusted labour force.

Seasonal factor used for adjusting the unemployment rate



Note : When the seasonal factor exceeds 100%, there will be downward effect on the unemployment rate after seasonal adjustment, and vice-versa.

While the published unemployment rate is seasonally adjusted as such, the published figures on labour force, employed persons and unemployed persons are not seasonally adjusted, so as to directly reveal the actual numbers in the respective categories within the population of Hong Kong.

/Table 5.2

Table 5.2

**The labour force, and persons employed,
unemployed and underemployed**

	<u>Labour force</u>	<u>Persons employed</u>	<u>Persons unemployed^(a)</u>	<u>Persons underemployed</u>
2002 Annual	3 487 100 (1.8)	3 231 600 (-0.6)	255 500	105 200
Q1	3 457 600 (1.6)	3 219 000 (-1.1)	238 600	109 200
Q2	3 466 500 (1.6)	3 203 100 (-1.7)	263 400	100 600
Q3	3 517 000 (2.1)	3 249 000 (-0.3)	268 000	101 500
Q4	3 507 400 (1.6)	3 255 300 (0.5)	252 100	109 400
2003 Q1	3 503 500 (1.3)	3 243 700 (0.8)	259 800	100 700
Q2	3 519 500 (1.5)	3 219 400 (0.5)	300 000	151 000
Q3	3 492 000 (-0.7)	3 194 800 (-1.7)	297 300	126 600
	<-0.8>	<-0.8>		
May - Jul	3 510 800 (0.3)	3 201 500 (-0.8)	309 200	148 700
Jun - Aug	3 510 700 (-0.1)	3 201 300 (-1.1)	309 400	141 500
Jul - Sep	3 492 000 (-0.7)	3 194 800 (-1.7)	297 300	126 600
	<-0.8>	<-0.8>		

Notes : (a) These include first-time job-seekers and re-entrants into the labour force.

() % change over a year earlier.

< > % change over the preceding quarter.

Source : General Household Survey, Census and Statistics Department.

Table 5.3

**Median duration of unemployment and
proportion of the unemployed population
by duration of unemployment**

		<u>Proportion unemployed for :</u>			
		<u>Median duration of unemployment (Days)</u>	<u>Less than 3 months (%)</u>	<u>3 months to less than 6 months (%)</u>	<u>6 months or more (%)</u>
2002	Annual	87	52	19	29
	Q1	86	53	20	27
	Q2	89	51	19	30
	Q3	82	55	17	28
	Q4	90	51	19	30
2003	Q1	82	54	17	29
	Q2	82	54	18	28
	Q3	90	50	19	31

Note : Figures may not add up exactly to the total due to rounding.

Source : General Household Survey, Census and Statistics Department.

/Table 5.4

Table 5.4

**Median hours of work per week and
proportion of the employed population
by hours of work per week**

		Median hours of work per week for all employed persons (Hours)	<u>Proportion of employed persons working for :</u>		
			<u>35 - 49 hours per week (%)</u>	<u>50 hours or more per week (%)</u>	<u>60 hours or more per week (%)</u>
2002	Annual	48	51	38	22
	Q1	46	52	34	20
	Q2	48	52	36	21
	Q3	48	50	40	22
	Q4	48	50	40	24
2003	Q1	48	46	38	23
	Q2	45	49	36	22
	Q3	48	49	40	23

Note : Figures may not add up exactly to the total due to rounding.

Source : General Household Survey, Census and Statistics Department.

5.4 On a quarter-to-quarter comparison, *total employment*⁽³⁾ as enumerated from households was reduced further, by 0.8% in the third quarter of 2003, following a 0.7% decrease in the second quarter. Weakened labour demand in manufacturing and in foundation and superstructure construction was a major contributory factor. The former could be due to further relocation of production processes outside Hong Kong, and the latter due to completion or winding down of some major construction projects. Yet employment gains were still found in quite a number of economic sectors including restaurants, real estate, the wholesale trade and business services, along with the pick-up in business activity. As to labour supply, *total labour force*⁽⁴⁾ showed a distinct moderation, to a 0.8% decrease in the third quarter of 2003, from a 0.5% increase in the second quarter. This reflected the combined influence of a contraction in the population of working age and a decline in the labour force participation rate⁽⁵⁾ especially for middle-aged females. On a year-on-year comparison, total employment and total labour force both fell, by 1.7% and 0.7% respectively in the third quarter of 2003, having expanded by 0.5% and 1.5% in the second quarter.

/Box 5.2

Box 5.2**Employment growth differentiated by
employment status in recent years**

During 1998 to 2002, total employment expanded cumulatively by 3.5%, or by an annual average of 0.9%, from 3.12 million to 3.23 million. But the growth rate varied amongst persons with different employment status.

**Employed persons by employment status
(year-on-year rate of change (%))**

	Total employment	Within which :			Unpaid family workers
		Employees	Employers	Self-employed persons	
1998	-1.3	-1.3	-4.4	4.2	-8.3
1999	-0.3	-0.9	-1.5	8.8	23.1
2000	3.1	3.4	-2.3	4.0	-11.9
2001	1.4	-0.1	5.4	24.7	3.9
2002	-0.6	-1.7	-2.4	14.4	10.6

The number of self-employed persons, whilst on a continuous uptrend in recent years, increased rather more distinctly in 2001 and 2002. Reduced vacancies in the corporate sector and growing tendency towards outsourcing induced more people to become self-employed. On the other hand, the number of employees was mostly on a decline, as overall labour demand slackened amidst moderate economic performance for most of the period and increased incidents of corporate downsizing and lay-offs. The number of employers also fell, amidst a more stringent business climate. As to unpaid family workers, the movements were more volatile, but the absolute number of people involved was rather small.

As a result, the proportion of employees in total employment fell over the period, from 89.7% in 1998 to 87.2% in 2002. So did the proportion of employers, from 5.2% to 5.0%. By contrast, the proportion of self-employed persons went up appreciably, from 4.6% to 7.2%. The proportion of unpaid family workers held broadly stable, at around 0.7%.

/Diagram 5.2

Diagram 5.2

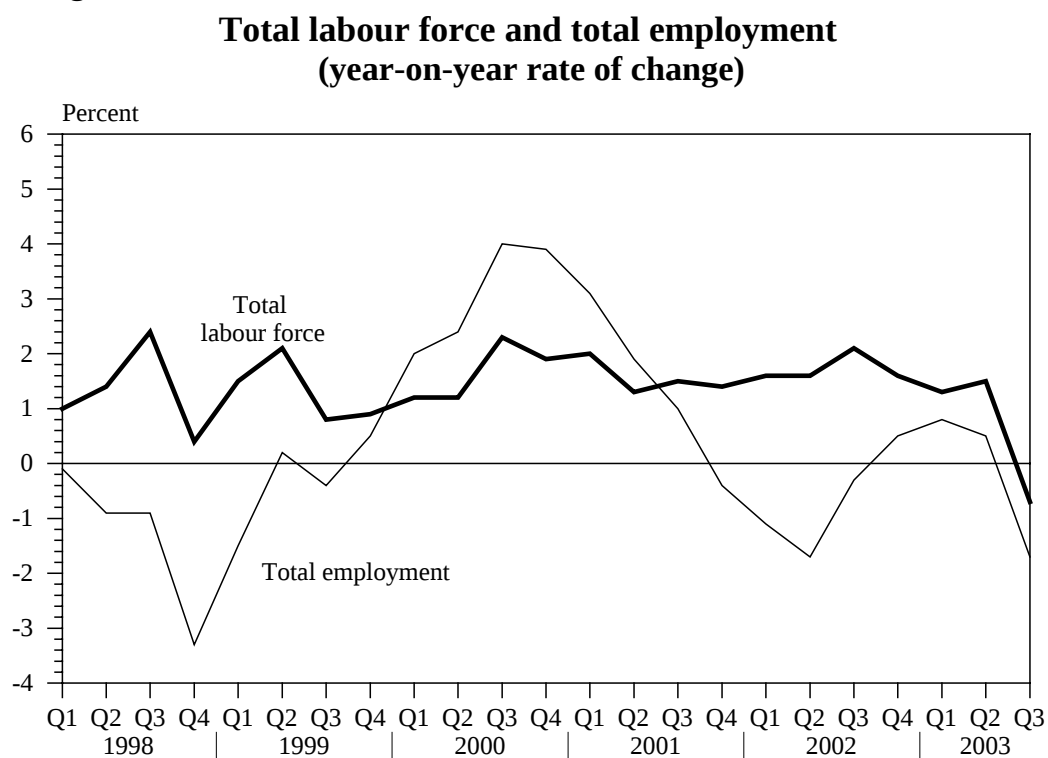


Table 5.5

Labour force participation rates by sex (%)

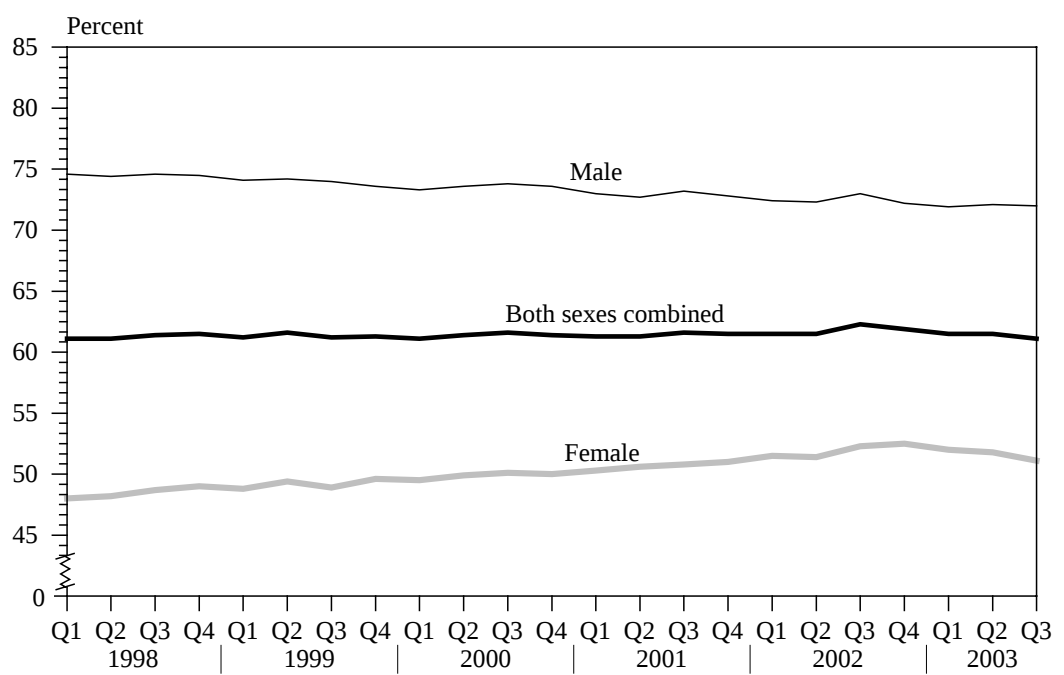
		<u>Male</u>	<u>Female</u>	<u>Both sexes combined</u>
2002	Annual	72.5	51.9	61.8
	Q1	72.4	51.5	61.5
	Q2	72.3	51.4	61.5
	Q3	73.0	52.3	62.3
	Q4	72.2	52.5	61.9
2003	Q1	71.9	52.0	61.5
	Q2	72.1	51.8	61.5
	Q3	72.1	51.3	61.2

Source : General Household Survey, Census and Statistics Department.

/Diagram 5.3

Diagram 5.3

Labour force participation rates by sex



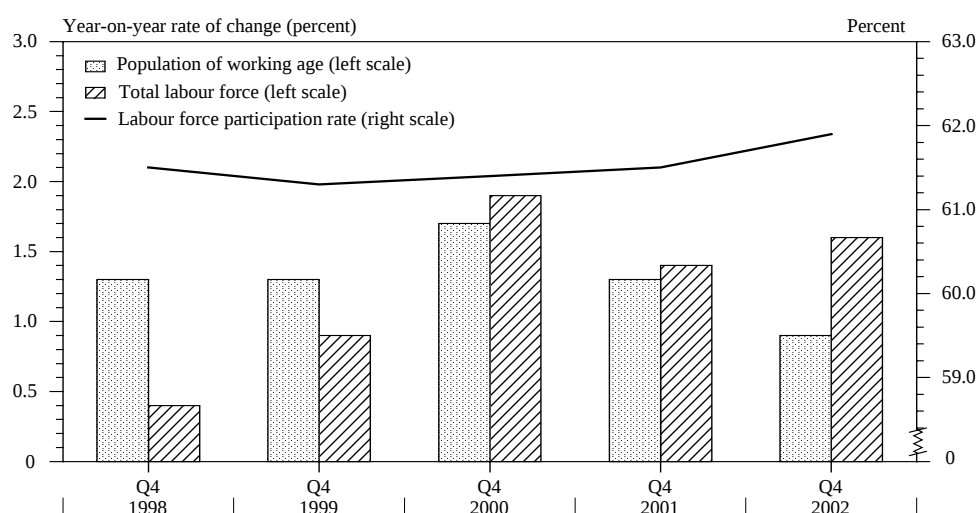
/Box 5.3

Box 5.3

Sources of growth in labour force in recent years

Between end-1998 and end-2002, total labour force increased from 3.31 million to 3.51 million, or by an annual average of 1.5%. This was largely attributable to an expansion in the population of working age (i.e. persons aged 15 and above), by an annual average of 1.3%. Yet a rise in the labour force participation rate also contributed.

Sources of growth in total labour force



The growth in the population of working age over the past four years was supported by both natural increase in the indigenous population and net inflow of people into Hong Kong. Yet the contribution to the overall growth over the period by indigenous increase, at 74.4%, was much larger than that by net inflow, at 25.6%. Net inflow comprised mainly foreign domestic helpers and other expatriate workers, as well as one-way permit holders from the mainland of China.

On the rise in the labour force participation rate (LFPR), it was entirely due to a surge in LFPR for females, mostly those aged 25-59, which more than offset a sustained decline in LFPR for males. Improved educational attainment, marriage postponement, and increased prevalence of spinsterhood were apparently the key factors pushing LFPR for females higher. Also, there appeared to be a greater proportion of married women entering the labour market for jobs in order to supplement family income, especially in 2001 and 2002 when there was an economic downturn.

/5.5

5.5 Labour income drifted lower in the second quarter, as the labour market slackened distinctly further under the adverse impact of SARS. Specifically, *labour earnings*⁽⁶⁾ decreased by 2.5% in money terms in the second quarter of 2003 from a year earlier, after a 2.0% drop in the first quarter. Netting out the decline in consumer prices as measured by the Composite CPI, labour earnings were down by only 0.1% in real terms in the second quarter of 2003 from a year earlier, having shown nil change in the first quarter. Likewise, *labour wages*⁽⁷⁾ were reduced by 2.5% in money terms in June 2003 from a year earlier, following a 1.5% fall in March. Netting out the decline in consumer prices as measured by the CPI(A), labour wages receded also by only 0.1% in real terms in June 2003, following a 0.3% rise in March.

5.6 In response to the outbreak of SARS and to prepare for the entry of school leavers into the labour market in the summer, the Government rolled out two employment-cum-training packages in May and July 2003 respectively, resulting in the creation of 53 550 employment/training openings at a total cost of \$1.15 billion. Of these openings, 30 550 were short-term employment and 23 000 were training openings. The \$432 million package launched in May comprised 11 500 temporary employment related opportunities and 10 000 training places under the Skills Enhancement Project. The majority of the initiatives under this package have been successfully concluded. The \$715 million package launched in July comprised 16 initiatives, with eight initiatives catering specifically for youths. Amongst the openings created, 19 050 were employment related, while 13 000 were training places (6 000 under the Youth Pre-employment Training Programme for youths and 7 000 under the Skills Enhancement Project for adults). Most of the vacancies thus generated had been filled by the beginning of September and the remaining ones would be filled shortly.

/Profile

Profile of unemployment and underemployment

5.7 Analysed by *economic sector*, distinct decreases in unemployment rate were observed in the tourism and consumption-related sectors between the second and third quarters of 2003, underpinned by the strong upsurge in incoming visitors and steady revival in consumer spending after SARS. This was particularly so for transport services, the retail trade, and restaurants and hotels. Meanwhile, the unemployment rate in the manufacturing sector also went down visibly. As to the underemployment rate, declines were again concentrated in restaurants and hotels, transport services and the retail trade, where many employees, having earlier been suspended from work or asked to take no-pay leave, had returned to their jobs. A large drop was also seen in construction.

Table 5.6

Unemployment rates by major economic sector (%)^(a)

	<u>2002</u>					<u>2003</u>		
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
Wholesale, retail and import/export trades, restaurants and hotels	7.8	7.4	8.3	7.7	7.9	7.9	9.1	8.7
Transport, storage and communications	5.4	5.6	5.3	5.3	5.4	6.1	7.6	6.2
Financing, insurance, real estate and business services	4.7	4.9	4.5	4.6	4.7	4.5	5.6	5.4
Community, social and personal services	3.2	2.7	3.3	3.5	3.1	2.9	3.7	3.7
Manufacturing	7.3	7.2	8.2	7.1	6.6	7.3	8.4	7.3
Construction ^(b)	15.8	15.7	16.8	15.6	15.2	18.9	19.7	19.6

Notes : (a) Not seasonally adjusted, and not including first-time job-seekers and re-entrants into the labour force.

(b) Including both site and non-site workers.

Source : General Household Survey, Census and Statistics Department.

/Table 5.7

Table 5.7**Underemployment rates by major economic sector (%)**

	<u>2002</u>					<u>2003</u>		
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
Wholesale, retail and import/export trades, restaurants and hotels	1.8	1.8	1.6	1.8	1.7	1.9	3.2	2.3
Transport, storage and communications	3.0	3.1	3.0	2.5	3.4	3.3	6.2	5.1
Financing, insurance, real estate and business services	0.6	0.7	0.5	0.6	0.5	0.7	0.9	0.7
Community, social and personal services	2.1	2.3	1.8	2.1	2.0	2.3	2.8	2.5
Manufacturing	2.5	2.4	2.6	2.3	2.6	1.8	3.6	3.7
Construction ^(a)	13.8	14.2	13.7	12.8	14.6	11.2	15.8	14.3

Note : (a) Including both site and non-site workers.

Source : General Household Survey, Census and Statistics Department.

/Table 5.8

Table 5.8

**Unemployment and underemployment rates
by detailed economic sub-sector in the third quarter of 2003**

	Unemployment rate ^(a) (%)	Numbers unemployed ^(a)	Underemploy- ment rate (%)	Numbers underemployed
Wholesale, retail and import/export trades, restaurants and hotels	8.7	93 800	2.3	24 400
Wholesale/retail trade	9.5	34 700	2.8	10 400
Import/export trade	5.0	21 800	0.7	3 000
Restaurants and hotels	13.8	37 300	4.1	11 000
Transport, storage and communications	6.2	22 900	5.1	19 000
Transport	6.2	19 100	5.8	17 800
Storage	5.5	300	3.7	200
Communications	6.3	3 500	1.9	1 000
Financing, insurance, real estate and business services	5.4	27 100	0.7	3 600
Financing	3.2	4 200	0.4	500
Insurance	4.6	1 900	0.8	300
Real estate	6.7	8 100	0.7	900
Business services	6.2	12 900	0.9	1 900
Community, social and personal services	3.7	32 800	2.5	22 100
Public administration	0.9	1 200	0.4	600
Education, medical and other health and welfare services	2.9	9 200	1.6	5 000
Other services	5.4	22 500	3.9	16 500
Manufacturing	7.3	21 100	3.7	10 700
Food and beverages	7.6	1 900	2.8	700
Clothing and footwear	9.5	7 200	7.6	5 800
Paper and printing	6.8	4 000	1.8	1 100
Plastic products	5.3	1 000	2.7	500
Metal products	5.7	800	2.8	400
Electrical and electronic products	6.7	4 000	1.7	1 000
Other manufacturing industries	5.8	2 300	3.2	1 300
Construction	19.6	64 100	14.3	46 700
Foundation and superstructure	17.1	41 700	12.1	29 400
Decoration and maintenance	26.9	22 300	20.8	17 300

Notes : As the above figures are based on a sample survey, they are subject to sampling errors, more so for the finer breakdowns.

Figures may not add up exactly to the total due to rounding.

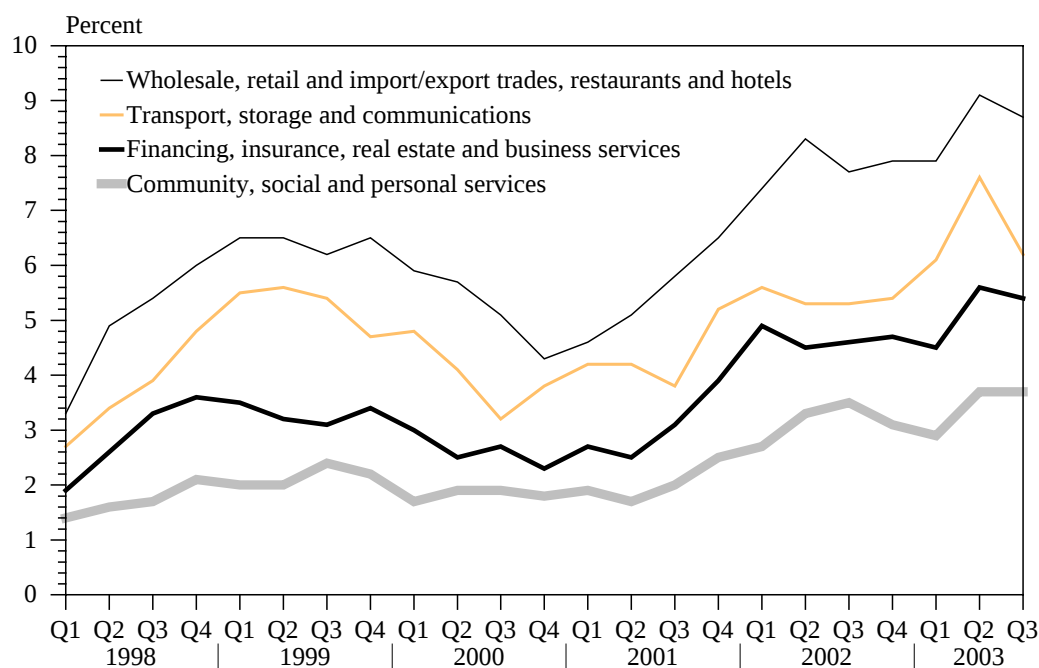
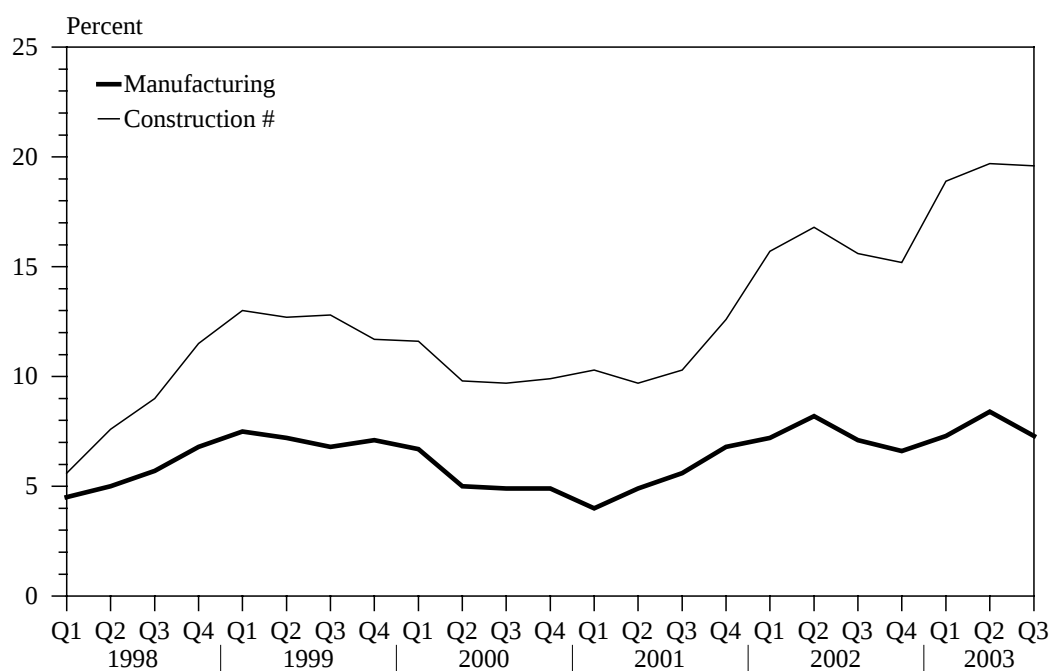
(a) Not seasonally adjusted, and not including first-time job-seekers and re-entrants into the labour force.

Source : General Household Survey, Census and Statistics Department.

/Diagram 5.4

Diagram 5.4

Unemployment rates by major economic sector*



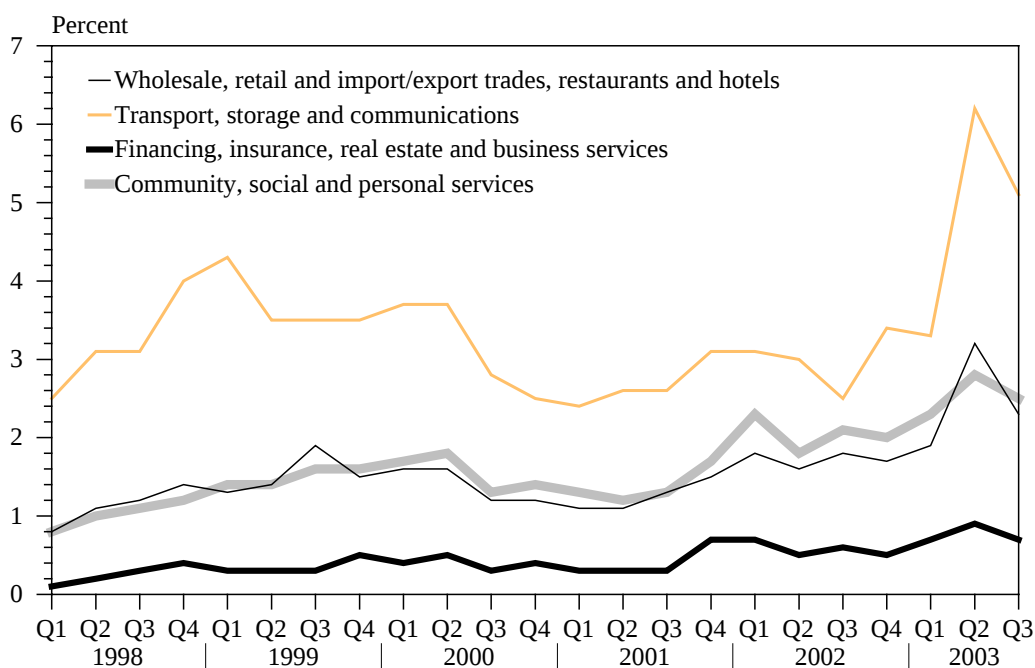
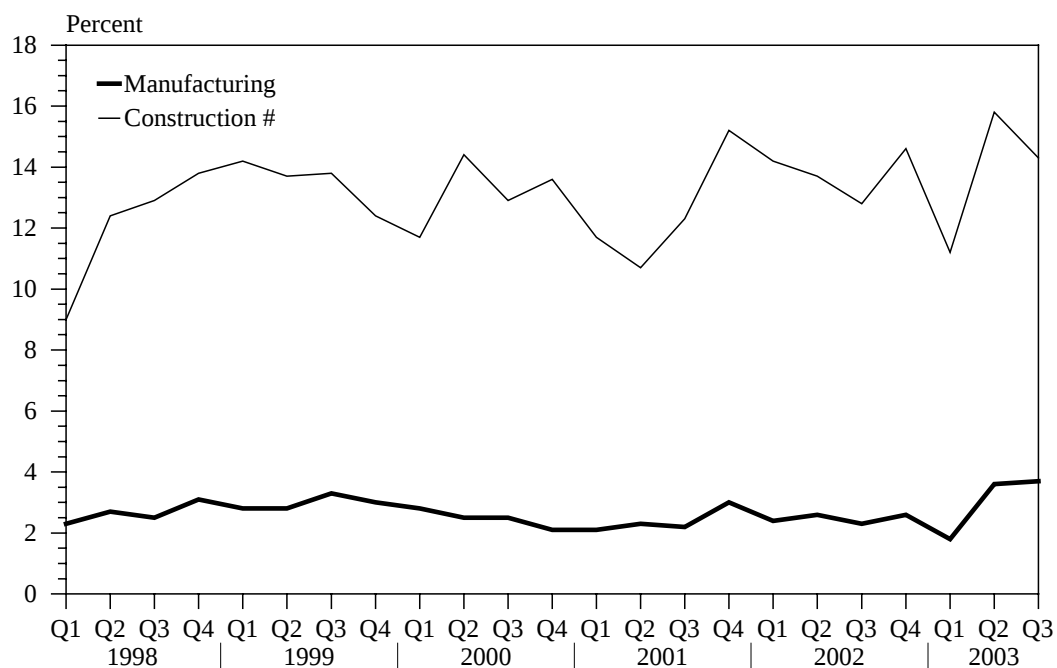
Notes : (*) Not seasonally adjusted, and not including first-time job-seekers and re-entrants into the labour force.

(#) Including both site and non-site workers.

/Diagram 5.5

Diagram 5.5

Underemployment rates by major economic sector



Note : (#) Including both site and non-site workers.

/5.8

5.8 Analysed by *occupation category*, the reduction in unemployment rate between the second and third quarters of 2003 took place mainly at the middle and lower segments of the occupational hierarchy. In line with the improved unemployment situation in the distributive and catering trades, there was a significant drop in the unemployment rate for service workers and shop sales workers, as well as for workers in elementary occupations. As to those at the upper segment of the occupational hierarchy, associate professionals had a noticeable fall in unemployment rate. On the underemployment rate, the decrease occurred across all the major occupation categories. Amongst them, service workers and shop sales workers, plant and machine operators and assemblers, craft and related workers, workers in elementary occupations, and associate professionals had relatively larger declines.

Table 5.9

Unemployment rates by major occupation category (%)^(a)

		<u>2002</u>					<u>2003</u>	
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
Managers and administrators	2.7	3.5	3.1	2.3	1.9	2.1	2.2	2.2
Professionals	2.4	2.6	2.5	2.3	2.1	2.2	2.8	2.8
Associate professionals ^(b)	4.3	4.2	4.3	4.5	4.3	4.3	4.9	4.6
Clerks	5.3	5.2	5.5	5.4	5.2	5.0	5.4	5.8
Service workers and shop sales workers	9.1	8.4	9.5	9.1	9.4	9.4	12.3	10.8
Craft and related workers	14.0	12.6	15.7	14.2	13.5	16.2	16.3	16.1
Plant and machine operators and assemblers	5.9	6.4	6.6	5.4	5.2	6.8	7.3	7.1
Elementary occupations	7.7	7.4	7.7	7.8	7.9	8.0	9.6	8.9
Others	3.4	2.4	2.9	4.7	3.8	4.6	1.6	6.8

Notes : (a) Not seasonally adjusted, and not including first-time job-seekers and re-entrants into the labour force.

(b) Including technicians and supervisors.

Source : General Household Survey, Census and Statistics Department.

/Table 5.10

Table 5.10**Underemployment rates by major occupation category (%)**

	<u>Annual</u>	<u>2002</u>				<u>2003</u>		
		<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
Managers and administrators	*	*	0	0.2	0	0.1	0.3	0.1
Professionals	0.3	0.4	0.3	0.3	0.2	0.3	0.6	0.5
Associate professionals ^(a)	0.8	0.8	1.0	0.8	0.7	0.9	1.6	1.1
Clerks	1.1	1.1	0.9	1.2	1.2	1.1	1.5	1.4
Service workers and shop sales workers	2.5	2.6	2.3	2.8	2.4	2.8	5.0	3.4
Craft and related workers	11.3	11.2	11.0	10.6	12.5	9.4	13.6	12.9
Plant and machine operators and assemblers	3.8	4.3	3.8	3.0	3.9	3.6	7.2	5.5
Elementary occupations	4.8	5.2	4.5	4.6	5.0	4.7	5.7	5.2
Others	3.5	0.8	6.8	5.8	0	1.0	10.1	1.3

Notes : (a) Including technicians and supervisors.

(*) Less than 0.05%.

Source : General Household Survey, Census and Statistics Department.

5.9 Analysed by sex, the unemployment rate for males went down by 0.3 of a percentage point to 9.8% in the third quarter of 2003, from 10.1% in the second quarter, whereas the unemployment rate for females went up by 0.4 of a percentage point to 6.9% from 6.5%. In consequence, the difference between the two unemployment rates narrowed from 3.6 percentage points to 2.9 percentage points between the two quarters. Meanwhile, the underemployment rates for males and females both descended, to 4.3% and 2.7% respectively in the third quarter of 2003, which were 0.8 and 0.6 of a percentage point below those of 5.1% and 3.3% in the second quarter. As a result, the difference between the two underemployment rates also narrowed, from 1.8 percentage points to 1.6 percentage points between the two quarters.

/Table 5.11

Table 5.11**Unemployment rates by sex (%)^(a)**

	<u>Male</u>	<u>Female</u>
2002 Annual	8.4	6.0
Q1	8.1	5.3
Q2	8.8	6.1
Q3	8.5	6.5
Q4	8.2	5.9
2003 Q1	8.7	5.8
Q2	10.1	6.5
Q3	9.8	6.9

Note : (a) Not seasonally adjusted, but including first-time job-seekers and re-entrants into the labour force.

Source : General Household Survey, Census and Statistics Department.

Table 5.12**Underemployment rates by sex (%)**

	<u>Male</u>	<u>Female</u>
2002 Annual	3.7	2.1
Q1	3.8	2.3
Q2	3.6	2.0
Q3	3.5	2.0
Q4	3.8	2.2
2003 Q1	3.4	2.2
Q2	5.1	3.3
Q3	4.3	2.7

Source : General Household Survey, Census and Statistics Department.

/5.10

5.10 Analysed by *age group*, persons aged 30-49 and aged 60 and above showed an appreciable drop in unemployment rate between the second and third quarters of 2003. Yet this was offset in part by a continued surge in the unemployment rate for younger persons aged 15-24, consequential to the entry of a new batch of fresh graduates and school leavers into the labour market. As regards underemployment, while an across-the-board decrease was observed, persons aged 15-19 and aged 40-59 were the ones having a larger decrease in underemployment rate.

Table 5.13

Unemployment rates by age group (%)^(a)

	<u>2002</u>					<u>2003</u>		
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
15-19	30.7	27.2	30.1	35.2	29.4	26.9	32.8	36.1
20-24	11.3	9.8	11.3	13.5	10.5	10.1	12.4	14.6
25-29	6.1	6.2	6.5	6.1	5.5	6.2	7.6	7.6
30-39	5.4	5.6	5.5	5.1	5.6	5.7	6.5	6.1
40-49	6.7	6.3	7.2	6.6	6.5	7.2	8.0	7.4
50-59	8.2	7.3	8.5	8.7	8.5	8.7	9.4	9.7
60 and above	5.0	5.3	6.0	4.6	4.2	3.6	5.3	3.6

Note : (a) Not seasonally adjusted, but including first-time job-seekers and re-entrants into the labour force.

Source : General Household Survey, Census and Statistics Department.

/Table 5.14

Table 5.14**Underemployment rates by age group (%)**

		<u>2002</u>				<u>2003</u>		
		<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
15-19	4.8	4.3	4.4	5.4	5.1	5.4	8.6	5.6
20-24	2.7	2.7	2.2	2.8	3.0	3.1	3.6	3.5
25-29	1.5	1.6	1.4	1.4	1.8	1.5	2.7	2.2
30-39	2.1	2.0	2.2	2.0	2.0	2.0	3.0	2.7
40-49	4.1	4.4	4.0	3.8	4.2	3.4	5.6	4.8
50-59	4.2	4.6	3.9	4.0	4.5	4.2	5.8	4.3
60 and above	3.1	3.6	3.0	2.8	2.8	3.3	3.1	2.8

Source : General Household Survey, Census and Statistics Department.

5.11 Analysed by *educational attainment*, the unemployment rate for persons with lower secondary education and below fell markedly between the second and third quarters of 2003. On the other hand, persons with tertiary education had a visible rise in unemployment rate, as the new batch of fresh graduates had yet to be fully absorbed into employment. As to underemployment, there was an extensive reduction across all the major educational attainment levels, with a sharper decrease for the lesser educated ones especially those with lower secondary education and below.

/Table 5.15

Table 5.15**Unemployment rates by educational attainment (%)^(a)**

	<u>2002</u>					<u>2003</u>		
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
No schooling/kindergarten	8.7	8.4	8.9	8.4	9.1	10.2	10.7	10.1
Primary	9.8	8.6	10.0	10.4	10.4	10.6	12.5	11.8
Lower secondary	10.9	10.4	11.4	10.5	11.1	11.5	13.2	12.2
Upper secondary ^(b)	6.9	6.6	7.3	7.2	6.5	7.0	7.9	7.9
Matriculation	5.2	5.1	5.4	5.1	5.3	5.1	5.9	5.9
Tertiary	4.3	3.9	4.2	5.1	4.0	3.8	4.4	5.5
<i>of which :</i>								
Non-degree	5.5	5.1	5.2	6.1	5.4	4.9	5.5	6.9
Degree	3.6	3.3	3.6	4.4	3.2	3.1	3.8	4.7

Notes : (a) Not seasonally adjusted, but including first-time job-seekers and re-entrants into the labour force.

(b) Including craft courses.

Source : General Household Survey, Census and Statistics Department.

/Table 5.16

Table 5.16**Underemployment rates by educational attainment (%)**

		<u>2002</u>				<u>2003</u>		
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
No schooling/kindergarten	7.1	7.8	7.2	6.8	6.4	8.3	11.2	6.7
Primary	6.4	6.9	6.5	5.9	6.5	6.2	7.9	6.8
Lower secondary	5.5	5.8	5.0	5.4	5.7	4.9	7.3	6.6
Upper secondary ^(a)	2.2	2.2	2.0	2.1	2.3	2.0	3.5	2.9
Matriculation	1.2	0.7	1.0	1.7	1.2	1.0	3.0	2.4
Tertiary	0.6	0.5	0.6	0.6	0.8	0.8	1.2	1.0
<i>of which :</i>								
Non-degree	0.9	0.5	1.0	0.9	1.3	1.2	1.7	1.2
Degree	0.4	0.5	0.4	0.4	0.4	0.6	0.9	0.8

Note : (a) Including craft courses.

Source : General Household Survey, Census and Statistics Department.

Profile of employment

5.12 Comparing June 2003 with a year earlier, total employment as enumerated from private sector establishments shrank by 3.8%, larger than the 2.5% decline in March. This was mainly attributable to the setback in business activity and thus labour demand during the second quarter, upon the impact of SARS. On a seasonally adjusted quarter-to-quarter comparison, total employment went down by 1.6% in June 2003, further to a 1.8% fall in March.

/5.13

5.13 Taking all the *service sectors* surveyed together⁽⁸⁾, employment was 2.2% fewer in June 2003 than a year earlier, exceeding the 1.4% fall in March. Analysed by constituent sector and on a year-on-year comparison, employment in storage and communications had the largest drop, by 15.1% in June 2003, amidst further rationalisation in the telecommunications sector. Employment in restaurants and hotels was also markedly reduced, by 10.6%, as the tourism and consumption-related sectors were hard hit by the outbreak of SARS. In a similar vein, employment in the retail trade was slashed by 4.3%. As regards water transport, air transport and services allied to transport, employment contracted by 6.1%, amidst another round of downsizing especially amongst the air ticket and travel agents caused by the outbreak of SARS. Employment in financing, insurance, real estate and business services fell relatively less, by 2.6%. By contrast, employment in community, social and personal services rose by 2.5%, led by increased labour demand in sanitary, welfare and education services. Employment in the wholesale and import/export trades had a small increase, by 0.4%, backed by the robust performance of external trade.

5.14 Employment in the local *manufacturing sector* kept on shrinking, by 13.8% in June 2003 over a year earlier, after a 9.4% drop in March. Continued contraction of domestic exports due to on-going relocation of production processes outside Hong Kong remained the major factor depressing labour demand in this sector.

5.15 Employment of manual workers at *building and construction sites* plummeted by 20.2% in June 2003 from a year earlier, having slid by 13.3% in March. Within the total, employment at private sector sites plunged by 27.4%. This was generally affected by the subdued property market. In particular, construction work on some residential and commercial development projects along the MTR Tung Chung Line tapered. Employment at public sector sites also contracted, by 9.5%. This was partly attributable to winding down or completion of some of the public housing re-development projects and school development projects. Also relevant was a high base of comparison in mid-2002, when construction activity at the KCR West Rail and the MTR Tseung Kwan O Extension was still intensive. Analysed by type of project, employment at civil engineering sites was reduced by 13.4%, and that at building sites even more by 22.8%. Taking into account off-site workers and related professional and support staff, employment in the entire building and construction sector⁽⁹⁾ had a relatively more moderate decline, by 5.4% in the second quarter of 2003 over a year earlier, following a 3.5% fall in the first quarter.

/5.16

5.16 In line with the Government's objective to cut operating expenditure and contain the size of the *Civil Service*, employment in the Civil Service was trimmed by 2.0% in June 2003 from a year earlier. This came after a 2.3% decrease in March. As stated in the Chief Executive's Policy Address on 8 January 2003, the Government plans to downsize the Civil Service establishment further to around 160 000 by 2006/07 through natural wastage. As from 1 April 2003, recruitment to the Civil Service is frozen. The Second Voluntary Retirement Scheme is implemented as another downsizing measure. Applications for the Scheme were received during 21 March - 20 May 2003, and the results were announced on 24 July. Out of 5 961 applications, 5 288 constituting 89% of the total were granted approval.

/Table 5.17

Table 5.17**Employment by major economic sector**

	Annual average	<u>2002</u>				<u>2003</u>	
		<u>Mar</u>	<u>Jun</u>	<u>Sep</u>	<u>Dec</u>	<u>Mar</u>	<u>Jun</u>
Wholesale and import/export trades	567 000 (-1.8)	566 100 (-2.6)	556 000 (-4.4)	580 400 (0.2)	565 300 (-0.3)	563 900 (-0.4)	558 200 (0.4)
Retail trade	216 800 (-1.3)	216 300 (0.4)	218 400 (-4.3)	221 300 (-1.7)	211 100 (0.4)	209 700 (-3.1)	209 000 (-4.3)
Restaurants and hotels	211 500 (-4.8)	213 600 (-3.2)	213 700 (-5.1)	212 300 (-4.8)	206 500 (-6.1)	198 200 (-7.2)	191 100 (-10.6)
Water transport, air transport and services allied to transport	101 000 (1.2)	100 800 (2.6)	102 300 (1.8)	101 000 (-0.6)	100 000 (0.9)	100 200 (-0.6)	96 100 (-6.1)
Storage and communications	40 100 (-9.8)	41 300 (-7.2)	41 600 (-9.7)	40 500 (-7.3)	36 900 (-14.9)	33 300 (-19.5)	35 300 (-15.1)
Financing, insurance, real estate and business services	429 900 (-1.3)	423 400 (-1.3)	430 300 (-2.8)	424 500 (-2.9)	441 300 (1.7)	422 500 (-0.2)	419 000 (-2.6)
Community, social and personal services	396 000 (5.9)	392 100 (8.8)	390 800 (4.9)	398 300 (5.7)	402 600 (4.5)	398 100 (1.5)	400 600 (2.5)
Manufacturing	193 000 (-9.0)	197 400 (-9.0)	200 100 (-8.5)	190 100 (-9.2)	184 500 (-9.1)	178 900 (-9.4)	172 500 (-13.8)
Building and construction sites	73 200 (-8.8)	76 900 (-12.4)	79 200 (-1.3)	70 400 (-8.0)	66 400 (-13.3)	66 700 (-13.3)	63 200 (-20.2)
<i>All establishments surveyed in the private sector^(a)</i>	<i>2 275 900 (-1.6)</i>	<i>2 275 500 (-1.1)</i>	<i>2 280 100 (-2.7)</i>	<i>2 286 100 (-1.5)</i>	<i>2 261 900 (-1.0)</i>	<i>2 219 000 (-2.5)</i>	<i>2 192 900 (-3.8)</i>
		<-0.4>	<-0.3>	<-0.3>	<-0.1>	<-1.8>	<-1.6>
<i>Civil Service^(b)</i>	<i>171 200 (-3.7)</i>	<i>173 000 (-4.4)</i>	<i>171 700 (-3.9)</i>	<i>170 500 (-3.5)</i>	<i>169 600 (-2.8)</i>	<i>169 100 (-2.3)</i>	<i>168 200 (-2.0)</i>

Notes : Employment figures enumerated from business establishments, as obtained from the Quarterly Survey of Employment and Vacancies, are somewhat different from those enumerated from households, as obtained from the General Household Survey. This is mainly due to difference in sectoral coverage: while the former survey covers selected major sectors, the latter survey covers all sectors in the economy.

(a) The total figures on private sector employment cover also employment in mining and quarrying and in electricity and gas supply, besides employment in the major sectors indicated above.

(b) These figures cover only those employed on Civil Service terms of appointment. Judicial officers, ICAC officers, locally engaged staff working in overseas Hong Kong Economic and Trade Offices, and other Government employees such as non-Civil Service contract staff are not included.

() % change over a year earlier.

< > Seasonally adjusted quarter-to-quarter % change.

Source : Quarterly Survey of Employment and Vacancies, Census and Statistics Department.

/Diagram 5.6

Employment by broad economic sector



Vacancies

5.17 Vacancies nevertheless showed a distinct improvement in the more recent period, as the impact on the labour market brought about by SARS began to ease. For all the private sector establishments surveyed taken together, although vacancies continued to go down on a year-on-year comparison, the decrease in June 2003 was much smaller than in March, by 4.9% as against 23.4%. On a seasonally adjusted quarter-to-quarter comparison, vacancies bounced up visibly by 33.2% in June 2003, reversing the 19.9% plunge in March. In consequence, the overall vacancy rate in the private sector moved higher, to 0.9% in June 2003, from 0.7% in March.

5.18 Analysed by *economic sector*, vacancies mostly fell, to various degree. For the *service sectors* taken together, the decrease in June 2003, by 3.9% over a year earlier, was again narrowed considerably from that in March, by 23.0%. Amongst the constituent sectors, vacancies in the retail trade and in restaurants and hotels fell the most, by 37.8% and 22.3% respectively in June 2003. Though with SARS faded, employers in these two sectors were still cautious about recruiting staff too soon. Vacancies in water transport, air transport and services allied to transport likewise still decreased markedly, by 17.7%, with the reduction mostly found in air passenger services. Meanwhile, vacancies in the wholesale and import/export trades had a much lesser decline, by 1.9%. On the other hand, vacancies in storage and communications, in community, social and personal services, and in financing, insurance, real estate and business services had renewed increases, by 14.3%, 11.0% and 3.2% respectively. As to the local *manufacturing sector*, vacancies dwindled by 16.4% in June 2003 over a year earlier, though lesser than the 23.5% reduction in March. Vacancies on *building and construction sites* continued to show the sharpest fall amongst all the sectors, with a 52.6% dip in June 2003 over a year earlier after a 81.7% slump in March. Vacancies in the *Civil Service* went down visibly further, by 13.5% in June 2003 over a year earlier, having been cut by 3.8% in March.

/Table 5.18

Table 5.18**Vacancies by major economic sector**

	<u>No. of vacancies</u>							
	<u>Annual average</u>	<u>2002</u>				<u>2003</u>		<u>Vacancy rate in Jun 2003 (%)</u>
		<u>Mar</u>	<u>Jun</u>	<u>Sep</u>	<u>Dec</u>	<u>Mar</u>	<u>Jun</u>	
Wholesale and import/export trades	4 400 (-7.1)	5 000 (-32.2)	5 000 (9.5)	4 200 (3.5)	3 500 (15.0)	4 400 (-12.2)	4 900 (-1.9)	0.9
Retail trade	1 800 (-14.3)	1 700 (-31.4)	2 500 (20.0)	1 600 (-33.1)	1 500 (-4.0)	1 100 (-35.1)	1 500 (-37.8)	0.7
Restaurants and hotels	1 300 (-13.8)	1 600 (-28.5)	1 400 (4.7)	1 400 (-10.8)	1 100 (-11.9)	800 (-47.0)	1 100 (-22.3)	0.6
Water transport, air transport and services allied to transport	500 (-24.3)	500 (-48.3)	600 (-21.6)	500 (17.2)	400 (-17.7)	400 (-9.7)	500 (-17.7)	0.5
Storage and communications	400 (-26.1)	400 (-31.0)	400 (-15.7)	400 (-11.3)	300 (-42.9)	300 (-25.6)	400 (14.3)	1.3
Financing, insurance, real estate and business services	5 200 (-18.6)	5 400 (-34.6)	6 000 (-22.3)	4 800 (-8.4)	4 600 (6.3)	4 200 (-22.1)	6 200 (3.2)	1.5
Community, social and personal services	4 100 (-26.5)	4 400 (-23.5)	4 200 (-35.4)	4 200 (-23.8)	3 700 (-20.9)	3 300 (-23.8)	4 600 (11.0)	1.1
Manufacturing	1 300 (-16.6)	1 400 (-25.0)	1 500 (-22.0)	1 400 (3.9)	900 (-17.9)	1 100 (-23.5)	1 200 (-16.4)	0.7
Building and construction sites	100 (-43.5)	100 (-42.7)	100 (-48.6)	100 (-19.7)	# (-62.7)	# (-81.7)	# (-52.6)	*
<i>All establishments surveyed in the private sector^(a)</i>	<i>19 400 (-17.5)</i>	<i>20 800 (-30.8)</i>	<i>21 900 (-14.9)</i>	<i>18 800 (-11.6)</i>	<i>16 200 (-5.5)</i>	<i>15 900 (-23.4)</i>	<i>20 800 (-4.9)</i>	<i>0.9</i>
		<i><-1.4></i>	<i><8.5></i>	<i><-10.5></i>	<i><-1.1></i>	<i><-19.9></i>	<i><33.2></i>	
<i>Civil Service^(b)</i>	<i>1 800 (3.3)</i>	<i>1 700 (9.0)</i>	<i>1 900 (16.0)</i>	<i>1 700 (1.9)</i>	<i>1 700 (-11.2)</i>	<i>1 600 (-3.8)</i>	<i>1 700 (-13.5)</i>	<i>1.0</i>

Notes : Vacancy rate refers to the ratio of vacancies to total employment opportunities (actual employment plus vacancies).

(a) The total figures on private sector vacancies cover also vacancies in mining and quarrying and in electricity and gas supply, besides vacancies in the major sectors indicated above.

(b) These figures cover only vacancies for those staff to be employed on Civil Service terms of appointment. They have been adjusted by deducting the vacant posts emerging from the First Voluntary Retirement Scheme.

() % change over a year earlier.

< > Seasonally adjusted quarter-to-quarter % change.

(*) Less than 0.05%.

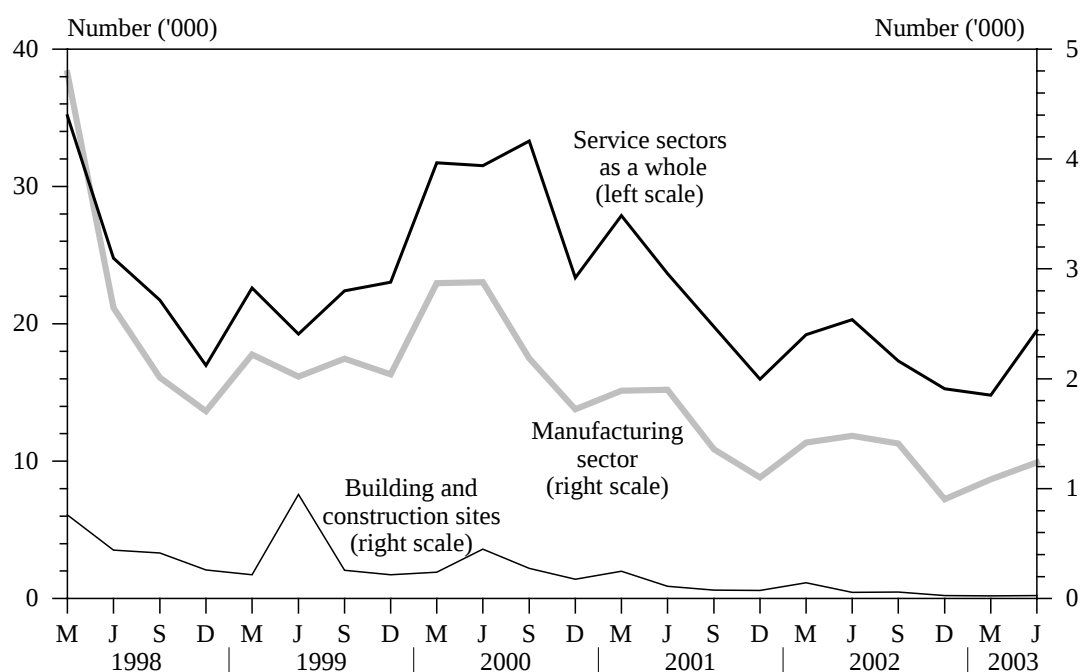
(#) Less than 50.

Source : Quarterly Survey of Employment and Vacancies, Census and Statistics Department.

/Diagram 5.8

Diagram 5.8

Vacancies by broad economic sector



5.19 Analysed by *occupation category*, vacancies for most of the categories either had a lesser decrease or reverted to increase in the more recent period. In the upper occupational segment, vacancies for associate professionals fell considerably less, by 0.5% in June 2003 over a year earlier, while vacancies for professionals even turned up to a distinct surge, by 21.5%. In contrast, vacancies for managers and administrators turned down to a fall, by 11.6% in June. In the middle and lower segments, vacancies for service workers and shop sales workers, plant and machine operators and assemblers, and craft and related workers all showed moderated declines, by 20.4%, 11.4% and 0.3% respectively in June 2003 over a year earlier. Vacancies for workers in elementary occupations were reduced by 16.1% in June, virtually the same as that in March. Vacancies for clerks rebounded to a mild increase, by 2.5% in June.

/Table 5.19

Table 5.19**Vacancies by major occupation category**

	<u>No. of vacancies</u>						
	<u>Annual average</u>	<u>2002</u>				<u>2003</u>	
		<u>Mar</u>	<u>Jun</u>	<u>Sep</u>	<u>Dec</u>	<u>Mar</u>	<u>Jun</u>
Managers and administrators	400 (-21.5)	400 (-48.7)	500 (-31.0)	500 (23.2)	400 (1.5)	500 (25.5)	400 (-11.6)
Professionals	1 100 (-39.1)	1 300 (-52.0)	1 100 (-53.5)	900 (-26.5)	1 100 (10.3)	1 100 (-12.9)	1 300 (21.5)
Associate professionals	6 900 (-5.8)	7 500 (-21.8)	8 300 (7.2)	6 400 (-4.1)	5 500 (1.7)	5 600 (-24.5)	8 200 (-0.5)
Clerks	3 800 (-32.4)	4 100 (-42.7)	4 200 (-37.9)	3 400 (-26.7)	3 400 (-9.7)	3 600 (-11.9)	4 300 (2.5)
Service workers and shop sales workers	3 700 (-8.1)	3 900 (-20.1)	3 900 (7.3)	3 800 (-4.4)	3 000 (-11.7)	2 300 (-41.9)	3 100 (-20.4)
Craft and related workers	500 (-27.8)	600 (-37.8)	600 (-13.9)	400 (-40.9)	500 (-9.0)	600 (-4.9)	600 (-0.3)
Plant and machine operators and assemblers	800 (-6.3)	900 (3.0)	700 (-31.9)	900 (22.5)	500 (-8.3)	400 (-54.4)	600 (-11.4)
Elementary occupations	2 300 (-17.8)	2 200 (-32.4)	2 700 (-8.0)	2 400 (-13.8)	1 800 (-13.7)	1 900 (-16.0)	2 200 (-16.1)

Note : () % change over a year earlier.

Source : Quarterly Survey of Employment and Vacancies, Census and Statistics Department.

/Earnings

Earnings and wages

5.20 Labour income in money terms drifted lower in the second quarter, as the labour market slackened distinctly further under the adverse impact of SARS. Overall *labour earnings* in the private sector, as measured by payroll per person engaged, fell by 2.5% in money terms in the second quarter of 2003 over a year earlier, widened further from the 2.0% decline in the first quarter. Amongst the business establishments surveyed in the second quarter of 2003, 47% reported a reduction in average labour earnings over a year earlier, while 24% cited virtually no change. The remaining 29% indicated a rise in average labour earnings, but this was partly due to an increase in the proportion of higher-skill and better-paid workers upon retrenchment of workers at the lower level. Netting out the decline in consumer prices as reflected by the Composite CPI, overall labour earnings slid marginally by 0.1% in real terms in the second quarter of 2003 from a year earlier, having held intact in the first quarter. On a seasonally adjusted quarter-to-quarter comparison, overall labour earnings edged lower by 0.7% in money terms in the second quarter of 2003, after a 1.0% decrease in the first quarter. In real terms, there was nevertheless a 0.3% rise in the second quarter of 2003, reversing the 0.6% fall in the first quarter.

5.21 Analysed by *economic sector*, labour earnings in money terms went down fairly extensively. Taking all the *service sectors* surveyed together, earnings sank by 3.0% in money terms in the second quarter of 2003 from a year earlier, following a 2.1% decline in the first quarter. Yet in real terms, they fell less, by 0.6% in the second quarter of 2003 over a year earlier, after a 0.1% decline in the first quarter. Analysed by constituent sector, earnings in restaurants and hotels were reduced most visibly, by 9.8% in money terms or 7.6% in real terms in the second quarter of 2003 over a year earlier. This was followed by earnings in community, social and personal services and in transport, storage and communications, with respective declines of 4.6% and 3.8% in money terms, or 2.2% and 1.4% in real terms. Earnings in the wholesale, retail and import/export trades slid by 2.5% in money terms, yet remained steady in real terms. Earnings in financing, insurance, real estate and business services were lowered by 1.5% in money terms, but still up by 0.9% in real terms. As to the local *manufacturing sector*, earnings continued to drop, by 2.2% in money terms in the second quarter of 2003 over a year earlier, although this was smaller than the 5.1% decrease in the first quarter. In real terms, earnings turned to a 0.3% rise in the second quarter of 2003 over a year earlier, from a 3.2% dip in the first quarter.

/Table 5.20

Table 5.20

**Labour earnings by major economic sector
(year-on-year rate of change (%))**

		Payroll per person engaged						
		2002				2003		Average amount in Q2 2003 (\$)
	Annual	Q1	Q2	Q3	Q4	Q1	Q2	
Wholesale, retail and import/export trades	-1.6 (1.4)	-1.0 (1.6)	-1.6 (1.7)	-2.1 (1.5)	-2.0 (1.0)	-1.3 (0.7)	-2.5 (*)	11,300
Restaurants and hotels	-4.2 (-1.1)	-4.9 (-2.3)	-5.5 (-2.4)	-3.0 (0.5)	-3.1 (-0.1)	-6.6 (-4.7)	-9.8 (-7.6)	7,600
Transport, storage and communications	-0.2 (2.9)	-1.9 (0.7)	1.5 (4.9)	-2.5 (1.0)	2.0 (5.1)	-0.3 (1.7)	-3.8 (-1.4)	17,100
Financing, insurance, real estate and business services	-2.2 (0.8)	-2.0 (0.6)	-2.6 (0.6)	-1.4 (2.2)	-2.9 (*)	-2.7 (-0.7)	-1.5 (0.9)	17,600
Community, social and personal services	-1.3 (1.9)	* (2.7)	0.1 (3.4)	-2.4 (1.2)	-2.7 (0.3)	-4.2 (-2.2)	-4.6 (-2.2)	18,400
Manufacturing	-1.2 (1.9)	-0.8 (1.8)	-0.6 (2.7)	-1.1 (2.6)	-2.2 (0.7)	-5.1 (-3.2)	-2.2 (0.3)	11,000
All sectors surveyed in the private sector	-1.1 (2.0)	-0.6 (2.1)	-1.0 (2.2)	-1.5 (2.1)	-1.2 (1.8)	-2.0 (*)	-2.5 (-0.1)	14,100
		<-0.2> {1.0}	<-0.2> {0.5}	<-0.5> {0.1}	<-0.3> {0.1}	<-1.0> {-0.6}	<-0.7> {0.3}	

Notes : Figures not in brackets represent percentage changes in money terms, while those in round brackets represent percentage changes in real terms.

< > Seasonally adjusted quarter-to-quarter % change in money terms.

{ } Seasonally adjusted quarter-to-quarter % change in real terms.

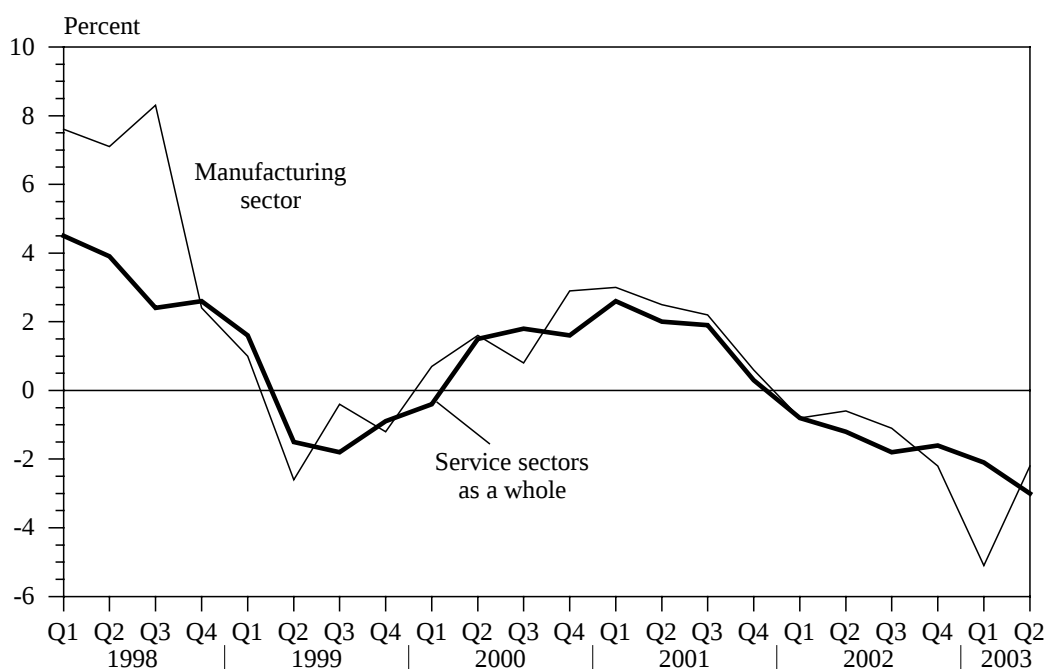
(*) Change of less than 0.05%.

Source : Labour Earnings Survey, Census and Statistics Department.

/Diagram 5.9

Diagram 5.9

**Earnings by broad economic sector
(year-on-year rate of change in money terms)**



5.22 Overall *labour wages* in the private sector also underwent a larger decrease in money terms in June 2003 than in March 2003, by 2.5% as against 1.5% over a year earlier. Amongst the business establishments surveyed in June 2003, 48% reported some downward adjustment in average wage rate from a year earlier, involving primarily a cut in guaranteed bonuses and allowances. Another 14% revealed nil change. The remaining 38% cited a rise in average wage rate, which again was partly attributable to a shift in employment composition towards better-paid workers upon retrenchment of the lower-paid clerical staff and operatives. Discounting the fall in consumer prices as measured by the CPI(A)⁽¹⁰⁾, overall labour wages edged lower by only 0.1% in real terms in June 2003 from a year earlier. This followed a slight increase of 0.3% in March.

5.23 Analysed by *economic sector*, restaurants and hotels were again the sector having a larger cut in wages, by 4.5% in money terms or 2.1% in real terms in June 2003 from a year earlier. The wholesale, retail and import/export trades and personal services had relatively smaller reductions in wages, by 2.9% and 2.8% respectively in money terms, or by 0.5% and 0.3% in real terms. For transport services, and financing, insurance, real estate and business services, wages went down by 2.0% and 0.9% respectively in money terms, yet still up by 0.4% and 1.5% in real terms. As to the local manufacturing sector, wages were slashed by 2.4% in money terms, but were virtually unchanged in real terms.

/Table 5.21

Table 5.21

**Wages by selected major economic sector
(year-on-year rate of change (%))**

	<u>By reference to the wage index</u>						
	<u>2002</u>					<u>2003</u>	
	<u>Annual</u>	<u>Mar</u>	<u>Jun</u>	<u>Sep</u>	<u>Dec</u> ^(a)	<u>Mar</u>	<u>Jun</u>
Wholesale, retail and import/export trades	-0.6 (1.7)	* (2.1)	0.3 (4.4)	-2.0 (2.4)	-0.7 (-1.7)	-1.2 (0.7)	-2.9 (-0.5)
Restaurants and hotels	-2.6 (-0.3)	-1.4 (0.6)	-3.3 (0.6)	-2.7 (1.6)	-3.0 (-4.0)	-3.2 (-1.4)	-4.5 (-2.1)
Transport services	0.6 (2.9)	1.1 (3.1)	0.8 (4.9)	* (4.4)	0.5 (-0.5)	-1.4 (0.4)	-2.0 (0.4)
Financing, insurance, real estate and business services	-0.8 (1.5)	-1.7 (0.3)	-1.8 (2.2)	* (4.4)	0.3 (-0.8)	0.3 (2.2)	-0.9 (1.5)
Personal services	-1.5 (0.8)	-0.9 (1.1)	-2.0 (2.0)	-3.0 (1.3)	-0.1 (-1.1)	-3.4 (-1.6)	-2.8 (-0.3)
Manufacturing	-1.4 (0.8)	-2.1 (-0.2)	-0.7 (3.4)	-1.5 (2.8)	-1.4 (-2.5)	-2.6 (-0.7)	-2.4 (*)
All selected sectors surveyed in the private sector	-1.0 (1.3)	-0.8 (1.2)	-0.9 (3.1)	-1.5 (2.8)	-0.8 (-1.8)	-1.5 (0.3)	-2.5 (-0.1)

Notes : Figures not in brackets represent percentage changes in money terms, while those in brackets represent percentage changes in real terms.

(a) Because of a low base of comparison in December 2001, due to the waiver of public housing rentals in that month, the CPI(A) had an upswing in December 2002, and this dampened the change in wages to decline in real terms across-the-board in December 2002 over a year earlier.

(*) Change of less than 0.05%.

Source : Labour Earnings Survey, Census and Statistics Department.

5.24 Analysed by *occupation category*, wages for miscellaneous non-production workers, service workers, clerical and secretarial workers, and operatives declined both in money terms and in real terms, by 2.7 - 4.0% and 0.3 - 1.6% respectively in June 2003 over a year earlier. Wages for supervisory and technical workers and for craftsmen fell to a lesser extent, by 1.8% and 0.8% respectively in money terms in June 2003 over a year earlier. In real terms, they were up modestly by 0.6% and 1.7%.

/Table 5.22

Table 5.22**Wages by selected major occupation category
(year-on-year rate of change (%))**

<u>By reference to the wage index</u>							
	<u>2002</u>					<u>2003</u>	
	<u>Annual</u>	<u>Mar</u>	<u>Jun</u>	<u>Sep</u>	<u>Dec</u> ^(a)	<u>Mar</u>	<u>Jun</u>
Supervisory and technical workers	-0.2 (2.1)	-0.2 (1.8)	0.1 (4.2)	-0.7 (3.7)	* (-1.0)	-0.2 (1.7)	-1.8 (0.6)
Clerical and secretarial workers	-1.1 (1.2)	-0.2 (1.8)	-0.8 (3.2)	-1.8 (2.5)	-1.7 (-2.7)	-2.2 (-0.4)	-3.0 (-0.6)
Craftsmen	-0.9 (1.4)	-0.6 (1.4)	-1.6 (2.4)	-1.5 (2.9)	0.2 (-0.8)	-1.5 (0.3)	-0.8 (1.7)
Operatives	-0.9 (1.4)	-1.0 (1.0)	0.1 (4.2)	-1.3 (3.0)	-1.3 (-2.3)	-2.7 (-0.9)	-2.7 (-0.3)
Service workers	-3.0 (-0.8)	-3.0 (-1.0)	-3.6 (0.3)	-3.4 (0.9)	-2.1 (-3.2)	-2.3 (-0.4)	-3.2 (-0.8)
Miscellaneous non-production workers	-1.3 (1.0)	-0.9 (1.1)	-1.4 (2.6)	-1.8 (2.6)	-1.0 (-2.1)	-2.8 (-1.0)	-4.0 (-1.6)

Notes : Figures not in brackets represent percentage changes in money terms, while those in brackets represent percentage changes in real terms.

(a) Also see Note (a) to Table 5.21.

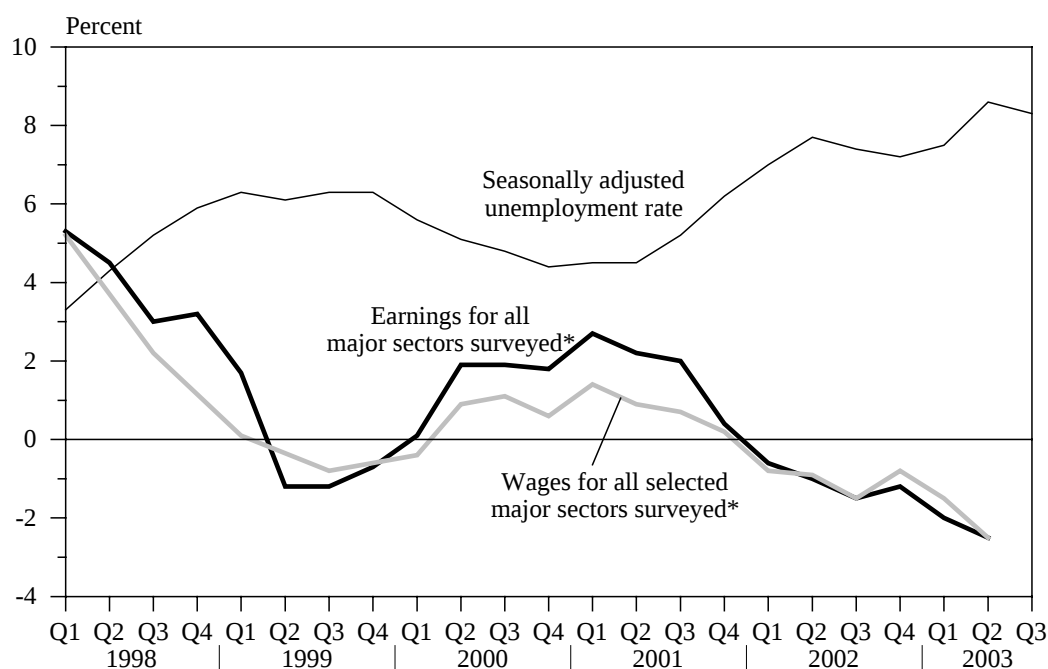
(*) Change of less than 0.05%.

Source : Labour Earnings Survey, Census and Statistics Department.

/Diagram 5.10

Diagram 5.10

Earnings, wages and the unemployment rate



Note : (*) Depicted as year-on-year rates of change in money terms.

5.25 Overall wages in the *construction sector* edged down by 1.0% in money terms in the second quarter of 2003 from a year earlier, having shown nil change in the first quarter. Nevertheless, netting out the fall in consumer prices as reflected by the CPI(A), construction wages rose by 0.8% in real terms in the second quarter of 2003 over a year earlier, further to a 1.8% increase in the first quarter.

5.26 Wages for the various constituent job categories continued to exhibit divergent movements. Specifically, wages for carpenters and joiners, concretors/bricklayers/drainlayers, plant operators, plasterers, steelbenders and electricians (wiremen) went down by 0.2 - 3.5% in money terms in the second quarter of 2003 over a year earlier, whereas wages for fitters, plumbers, painters and truck drivers went up by 0.4 - 2.7% in money terms.

/Table 5.23

Table 5.23

**Construction wage rates by selected job category
(year-on-year rate of change (%))**

		<u>2002</u>				<u>2003</u>	
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
Concretors/bricklayers/ drainlayers	0.4	-0.2	3.0	1.1	-2.0	*	-2.5
Steelbenders	2.2	1.0	3.1	3.4	1.4	-0.1	-1.1
Carpenters and joiners	3.0	-1.5	5.2	5.6	3.0	2.6	-3.5
Plumbers	-1.9	-3.8	-2.1	-2.3	0.6	1.1	1.9
Fitters	-0.8	2.6	-0.7	-2.4	-2.5	0.7	2.7
Plasterers	-1.8	-3.6	-1.9	-1.3	-0.3	-1.3	-1.3
Painters	-3.0	-2.1	-3.6	-4.5	-1.5	2.1	1.4
Electricians (wiremen)	1.9	3.3	2.7	0.3	1.4	1.4	-0.2
Plant operators	1.2	3.3	2.8	0.2	-1.4	-1.1	-1.5
Truck drivers	-0.3	2.5	1.3	-1.9	-2.8	-2.0	0.4
All job categories in the construction sector ^(a)	* (3.3)	-0.2 (2.6)	1.6 (5.3)	-0.4 (3.8)	-0.9 (1.6)	* (1.8)	-1.0 (0.8)

Notes : Figures not in brackets represent percentage changes in money terms, while those in brackets represent percentage changes in real terms.

(a) Apart from the above selected job categories, this also covers such other job categories as masons, blacksmiths, terrazzo and granolithic workers, glaziers, heavy load coolies, pneumatic drillers, bamboo workers and scaffolders, structural steel erectors, divers, and diver's linesmen. Yet as the employment involved in such job categories is much smaller, their respective wages are of lesser significance and are therefore not separately shown in this table.

(*) Change of less than 0.05%.

Source : Census and Statistics Department.

/5.27

5.27 In February this year, the Government announced its decision to restore the dollar value of all Civil Service pay points below Directorate Pay Scale 3 (D3) or equivalent to the levels as at 30 June 1997 by two adjustments of broadly equal amount to be implemented on 1 January 2004 and 1 January 2005 respectively, and to restore the dollar value of all Civil Service pay points at D3 and above or equivalent to the levels as at 30 June 1997 from 1 January 2004. This pay reduction will be implemented by legislation. Following consultation with staff representatives on the draft legislation, the Government gazetted the Public Officers Pay Adjustments (2004/2005) Bill on 16 May 2003 and introduced the Bill into the Legislative Council on 21 May 2003. It plans to have the Bill enacted before the end of 2003, so that the first stage of the Civil Service pay reduction can be implemented on 1 January 2004 as scheduled.

5.28 The Government has embarked on an exercise to develop, in consultation with staff, an improved Civil Service pay adjustment mechanism on the basis of the existing one. The improved mechanism will comprise the conduct of periodic pay level surveys to compare the Civil Service pay levels with those in the private sector, the conduct of annual pay trend surveys based on an improved methodology, and an effective means for implementing both upward and downward adjustments. To take forward the exercise, a steering committee has been established to tender advice in the process. Staff feedback is gauged through a consultative group comprising staff representatives. The aim is to complete the exercise, including the conduct of a pay level survey, by end-2004.

/Notes

Notes :

- (1) For a person aged 15 or above to be classified as unemployed, he or she should: (a) not have a job and not be performing any work for pay or profit during the reference period (i.e. seven days before enumeration); and (b) be available for work during the reference period; and (c) be seeking work during the 30 days before enumeration.

Notwithstanding the above, the following types of persons are also considered as unemployed: (a) persons without a job, having sought work but not available for work because of temporary sickness; (b) persons without a job, available for work but not having sought work because they will take up new jobs or start business at a subsequent date, or expect to return to their original jobs; and (c) discouraged workers not having sought work because they believe work is not available to them.

Even at full employment, some frictional unemployment is bound to exist as workers move between jobs in order to obtain better terms of employment. The precise level of unemployment which can be described as purely frictional varies amongst economies, depending on the structure and characteristics of their labour markets.

In April 2001, the Census and Statistics Department put out a revised series of seasonally adjusted unemployment rate compiled by reference to the X-11 ARIMA method, which adjusts for all seasonal variations in employment and unemployment (i.e. the changes due to holiday effects, seasonally ups and downs in economic activity, seasonal variations in first-time job-seekers, etc). This replaces the former series which adjusts only for seasonal variations in the proportion of first-time job-seekers in the labour force. For more details, see Note (3) at the end of Chapter 5 of the Half-yearly Economic Report 2001.

- (2) The main criteria for an employed person aged 15 or above to be classified as underemployed are: involuntarily working less than 35 hours during the reference period (i.e. seven days before enumeration), and either available for additional work during the reference period or seeking additional work during the 30 days before enumeration.

Following these criteria, employed persons taking no-pay leave due to slack work during the reference period are also classified as underemployed if they had worked less than 35 hours or were on leave for the entire reference period.

- (3) The employed population refers to those persons aged 15 or above who performed work for pay or profit or had a formal job attachment during the reference period (i.e. seven days before enumeration).
- (4) The labour force, or the economically active population, is defined to include all persons aged 15 or above who either were engaged in productive work during the reference period (i.e. seven days before enumeration) or would otherwise have been engaged in productive work but were unemployed.

/ (5)

- (5) The labour force participation rate is defined as the proportion of economically active population (i.e. those working or unemployed) in the population aged 15 or above.
- (6) In addition to wages, which include all regular payments like basic pay and stipulated bonuses and allowances, earnings also cover overtime pay and other non-guaranteed or irregular bonuses and allowances, except severance pay and long service payment. Because of this difference, as well as the difference in sectoral and occupational coverage, the movements in average earnings, as measured by payroll per person engaged, do not necessarily match closely with those in wage rates.
- (7) The wage data as collected have a more limited coverage than the corresponding earnings data. More specifically, the coverage of the service sectors in the wage data is far from complete, and the coverage of occupation categories in the wage data is only up to the supervisory and technical level.
- (8) The service sectors cover the wholesale, retail and import/export trades, restaurants and hotels; transport, storage and communications; financing, insurance, real estate and business services; and community, social and personal services.
- (9) Employment for the construction sector as a whole is enumerated from the General Household Survey carried out by the Census and Statistics Department. Apart from site workers, it also includes non-site workers engaged in minor alteration and addition, repair, maintenance and interior decoration work on existing buildings. In addition, it includes professional, administrative and other support personnel engaged in that sector, such as engineers, architects, surveyors and contract managers, as well as general clerical staff.
- (10) Different consumer price indices are used for compiling the real indices of labour earnings and wages, taking into account their relevance to the respective occupation coverage. Specifically, the Composite CPI, being an indicator of overall consumer prices, is taken as the price deflator for earnings received by employees at all levels of the occupational hierarchy. The CPI(A), being an indicator of consumer prices for the middle to lower income groups, is taken as the price deflator for wages in respect of workers on occupations up to the supervisory level, and also in respect of manual workers engaged in the construction sector.

CHAPTER 6 : PRICES

Consumer prices

6.1 Overall consumer prices declined further in the third quarter of 2003, thereby extending their downtrend to almost five years. Though with a pick-up in overall economic activity and improving consumer spending during the quarter, local retailers and service providers continued to restrain the prices of their goods and services. Price discounts and other concessions were still widespread, yet apparently with some modest narrowing by the end of the quarter. Meanwhile, the pressure on domestic costs remained scant, as property rentals and labour wages stayed subdued. In addition, there was a dampening effect on the respective costs to consumers brought about by the rates concession and the waiver of water and sewage charges granted by the Government for the periods July - September and August - November respectively⁽¹⁾. These factors taken together outweighed the pressure due to higher prices of retained imports brought about by a weaker US dollar and firmer world commodity prices.

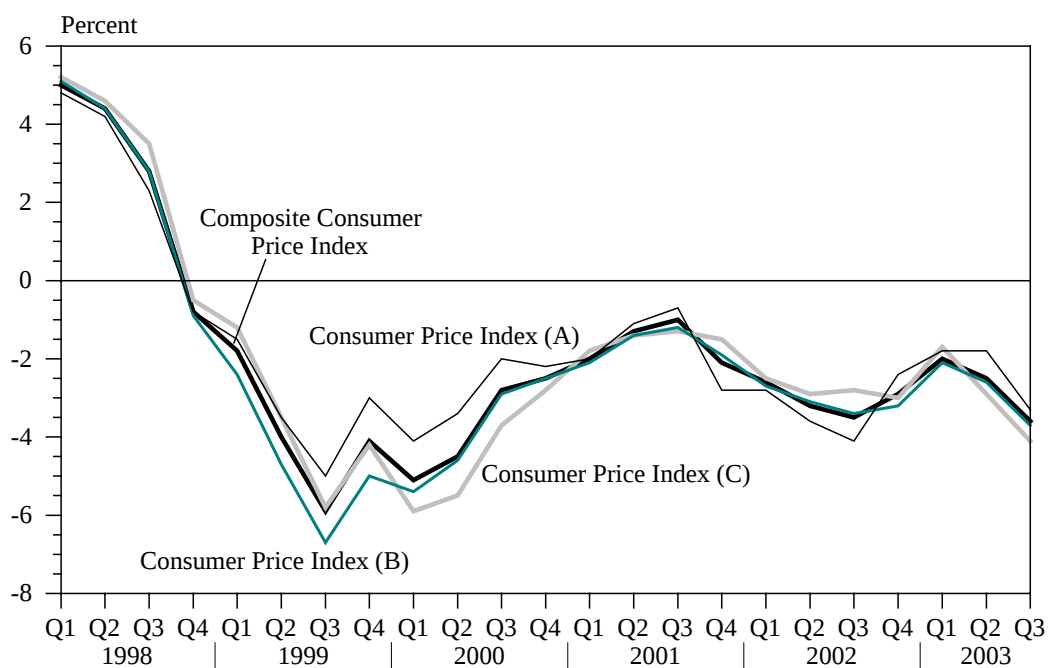
6.2 On a year-on-year comparison, the *Composite Consumer Price Index*⁽²⁾ went down by 3.6% in the third quarter of 2003, exceeding the 2.5% fall in the second quarter. The enlarged drop was mainly attributable to the Government's relief measures, specifically the rates concession and the waiver of water and sewage charges, which had the combined effect of lowering the Composite CPI by about one percentage point in the third quarter. For the first nine months of 2003 as a whole, the Composite CPI slid by 2.7% from a year earlier, which was nevertheless less than the 3.0% dip in 2002.

6.3 Analysed by sub-index, the CPI(A), CPI(B) and CPI(C) all moved lower, by 3.3%, 3.7% and 4.1% respectively in the third quarter of 2003 over a year earlier. These again exceeded the corresponding decreases in the second quarter, by 1.8%, 2.6% and 2.9%. For the first nine months of 2003 as a whole, the CPI(A), CPI(B) and CPI(C) fell by 2.3%, 2.8% and 2.9% respectively from a year earlier, as compared to declines of 3.2%, 3.1% and 2.8% in 2002.

/Diagram 6.1

Diagram 6.1

**Consumer Price Indices
(year-on-year rate of change)**



Note : From the fourth quarter of 2000 onwards, the year-on-year changes in the Consumer Price Indices are computed from the new 1999/2000-based CPI series. Before then, the changes are computed from the old 1994/95-based CPI series. Splicing has been applied to the indices to maintain continuity.

/Table 6.1

Table 6.1

**Consumer Price Indices
(year-on-year rate of change (%))**

		<u>Composite CPI</u>	<u>CPI(A)</u>	<u>CPI(B)</u>	<u>CPI(C)</u>
2002	Annual	-3.0	-3.2	-3.1	-2.8
	H1	-2.9	-3.2	-2.9	-2.7
	H2	-3.2	-3.3	-3.3	-2.9
	Q1	-2.6	-2.8	-2.7	-2.5
	Q2 ^(a)	-3.2	-3.6	-3.1	-2.9
	Q3	-3.5	-4.1	-3.4	-2.8
	Q4 ^(b)	-2.9	-2.4	-3.2	-3.0
2003	H1	-2.2	-1.8	-2.3	-2.3
	Q1-Q3	-2.7	-2.3	-2.8	-2.9
	Q1 ^(c)	-2.0	-1.8	-2.1	-1.7
	Q2	-2.5	-1.8	-2.6	-2.9
	Q3	-3.6	-3.3	-3.7	-4.1
	Jan	-1.6	-1.6	-1.7	-1.4
	Feb	-2.0	-2.0	-2.2	-1.9
	Mar	-2.1	-1.9	-2.3	-1.9
	Apr ^(d)	-1.8	-1.2	-2.0	-2.1
	May	-2.5	-1.7	-2.7	-3.0
	Jun ^(e)	-3.1	-2.4	-3.2	-3.7
	Jul ^(f)	-4.0	-3.6	-4.1	-4.5
	Aug	-3.8	-3.5	-3.9	-4.1
	Sep ^(g)	-3.2	-2.8	-3.2	-3.8

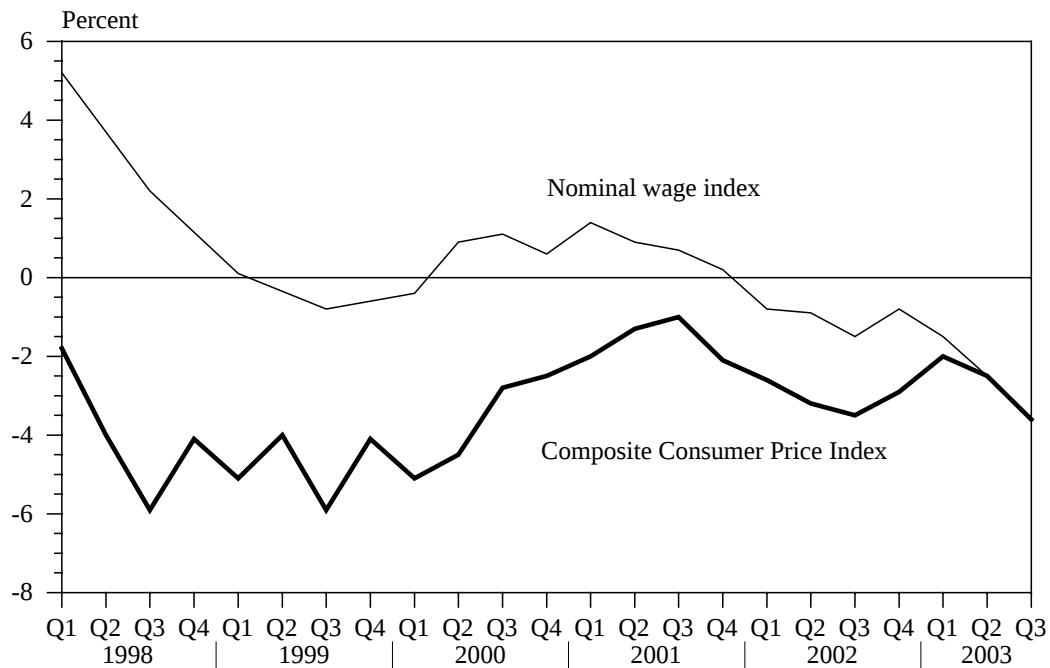
- Notes :
- (a) The widening in year-on-year decline in the CPIs in the second quarter of 2002 was due in part to the waiver of water and sewage charges as well as the additional rates concession granted by the Government as from April 2002.
 - (b) The narrowing in year-on-year decline in the Composite CPI, CPI(A) and CPI(B) in the fourth quarter of 2002 was mostly attributable to a lower base of comparison a year earlier, caused by the waiver of public housing rentals by the Housing Authority and Housing Society in December 2001. The CPI(C) was unaffected by such a measure, as public housing cost was irrelevant to this sub-index.
 - (c) The further narrowing in year-on-year decline in the CPIs in the first quarter of 2003 was mainly attributable to a lower base of comparison brought about by the rates concession by the Government in 2002.
 - (d) The smaller year-on-year decline in the Composite CPI, CPI(A) and CPI(B) in April than in March 2003 was mainly attributable to a lower base of comparison brought about by the waiver of water and sewage charges by the Government from April 2002 to March 2003. The CPI(C) was affected much less by such a measure.
 - (e) The larger year-on-year decline in the CPIs in June than in May 2003 was partly due to a special one-off rebate of electricity charges granted by a power company in June and July 2003.
 - (f) The further widening in year-on-year decline in the CPIs in July 2003 was largely attributable to the rates concession granted by the Government for the third quarter.
 - (g) The lesser year-on-year decline in the CPIs in September than in August 2003 was partly due to renewed increases in the prices of fresh vegetables and women's outerclothing, as well as in the charges for package tours. Also contributed was moderated decrease in the charges for telephone and other communications services.

/Diagram 6.2

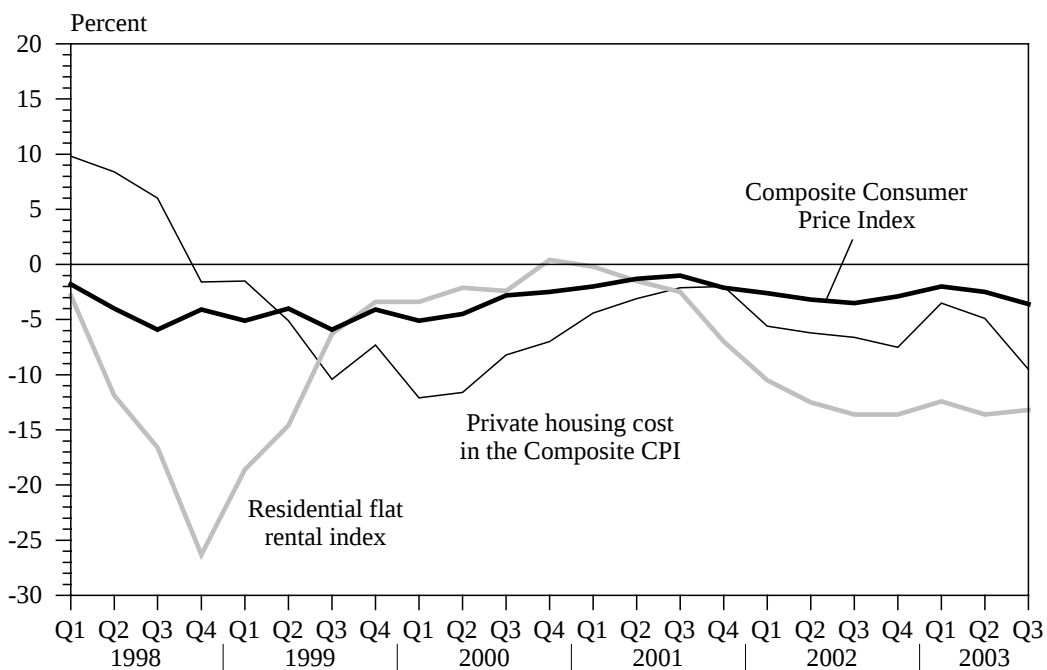
Diagram 6.2

**Composite Consumer Price Index vis-à-vis labour wages,
residential flat rentals, and prices of retained imports
(year-on-year rate of change)**

(a) Compared with labour wages



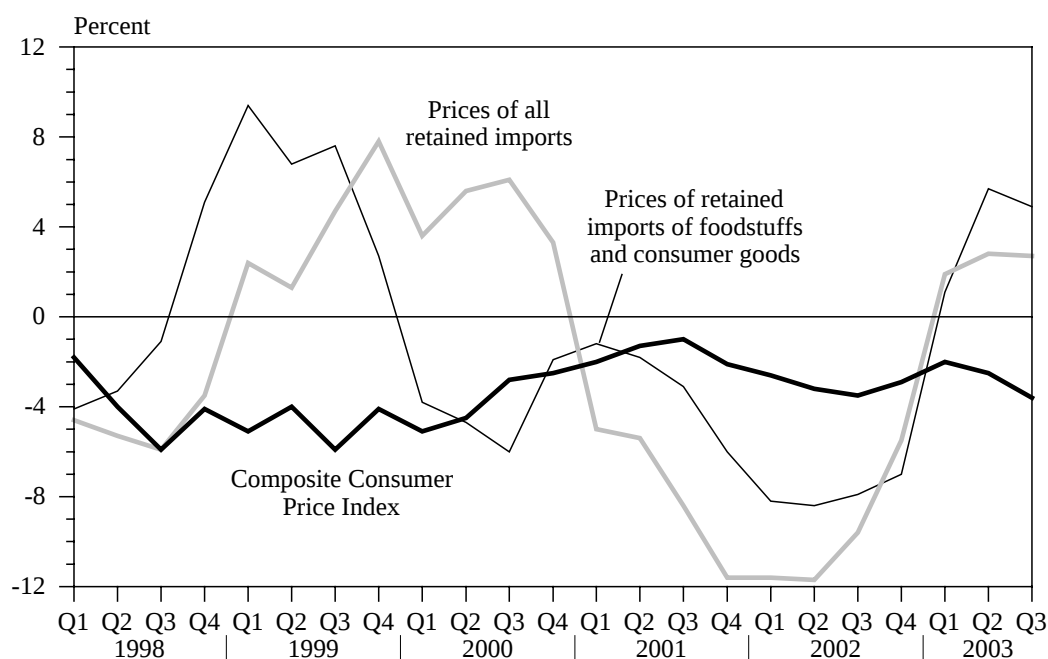
(b) Compared with residential flat rentals



/Diagram 6.2 (cont'd)

Diagram 6.2 (cont'd)

(c) Compared with prices of retained imports



Note : See the footnote to Diagram 6.1.

6.4 On a quarter-to-quarter comparison, the seasonally adjusted Composite CPI likewise showed an accentuated fall, from 1.1% in the second quarter of 2003 to 1.9% in the third quarter. The seasonally adjusted CPI(A) and CPI(B) exhibited a similar movement, with their declines widening from 0.5% and 1.1% respectively in the second quarter of 2003 to 2.3% and 1.8% in the third quarter. The Government's relief measures as mentioned were a major contributory factor. On the other hand, the seasonally adjusted CPI(C) had a moderated decrease, from 1.8% to 1.6% between the two quarters, as the downward effect from the Government's relief measures was more than offset by the lifting effect from renewed increases in the prices of clothing and footwear and of miscellaneous goods as well as from lesser declines in the prices of durable goods and in the charges for miscellaneous services.

/Table 6.2

Table 6.2

**Seasonally adjusted Consumer Price Indices
(quarter-to-quarter rate of change (%))**

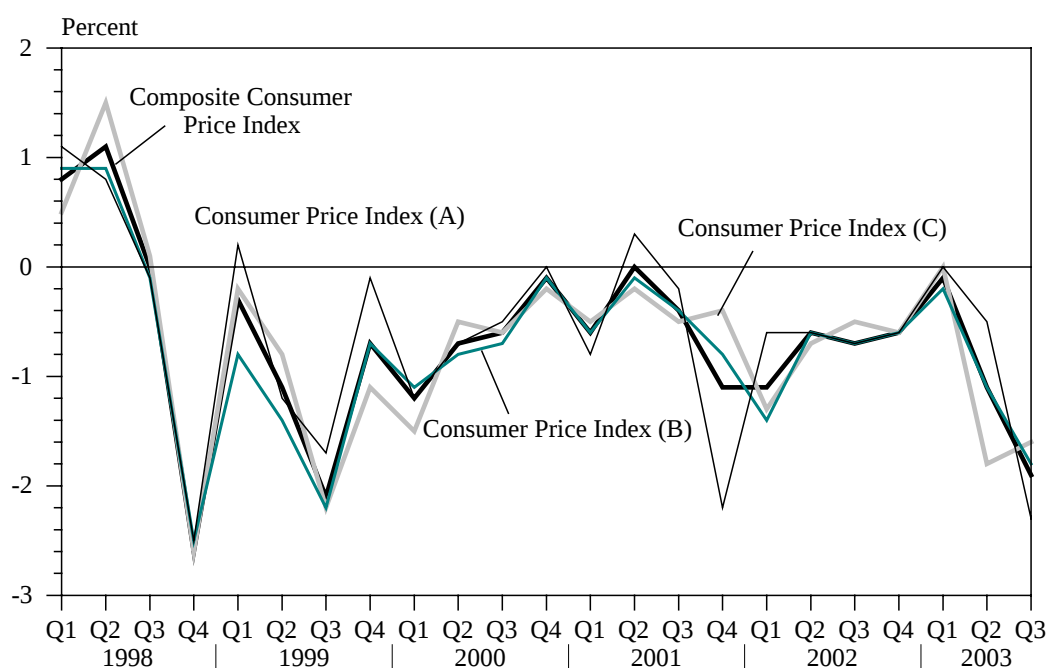
		<u>Composite CPI</u>	<u>CPI(A)</u>	<u>CPI(B)</u>	<u>CPI(C)</u>
2002	Q1	-1.1	-0.6	-1.4	-1.3
	Q2 ^(a)	-0.6	-0.6	-0.6	-0.7
	Q3	-0.7	-0.7	-0.7	-0.5
	Q4	-0.6	-0.6	-0.6	-0.6
2003	Q1 ^(b)	-0.1	*	-0.2	*
	Q2 ^(c)	-1.1	-0.5	-1.1	-1.8
	Q3 ^(d)	-1.9	-2.3	-1.8	-1.6

- Notes : (a) The quarter-to-quarter decline in the seasonally adjusted CPIs mostly narrowed in the second quarter of 2002. There was little additional dampening effect from the rates concession by the Government in the second quarter, given that the base of comparison in the first quarter was already lowered by that measure. Also, the effect of the special one-off rebate of electricity charges by a power company in the first two months of 2002 had dissipated. These outweighed the new dampening effect from the waiver of water and sewage charges granted by the Government for one year as from April 2002.
- (b) The quarter-to-quarter decline in the seasonally adjusted CPIs narrowed distinctly further in the first quarter of 2003. This was mainly attributable to dissipation of the downward effect of the rates concession by the Government in 2002, which outweighed the downward effect of the special one-off rebate of electricity charges granted by a power company in January and February 2003.
- (c) The quarter-to-quarter decline in the seasonally adjusted CPIs widened considerably in the second quarter of 2003, mainly reflecting the impact of SARS on consumer demand and hence consumer prices.
- (d) The quarter-to-quarter decline in the seasonally adjusted CPIs mostly enlarged further in the third quarter of 2003, mainly reflecting the downward effect of the rates concession and the waiver of water and sewage charges granted by the Government for the periods July - September and August - November respectively.
- (*) Change of less than 0.05%.

/Diagram 6.3

Diagram 6.3

**Seasonally adjusted Consumer Price Indices
(quarter-to-quarter rate of change)**



Note: From the first quarter of 2000 onwards, the quarter-to-quarter changes in the seasonally adjusted Consumer Price Indices are computed from the new 1999/2000-based CPI series. Before then, the quarter-to-quarter changes are computed from the old 1994/95-based CPI series. Splicing has been applied to the indices to maintain continuity.

6.5 Analysed by major *commodity group* in the Composite CPI and on a year-on-year comparison, the prices of basic foodstuffs came down by 1.5% in the third quarter of 2003. This exceeded the 1.3% fall in the second quarter, owing to enlarged decreases in the prices of certain food items like fish, processed sea products and non-alcoholic beverages. The charges for meals at restaurants were reduced by 1.6% in both quarters, as restaurant operators continued to stimulate business through price cuts. The cost of transport was lowered by 0.8% in the third quarter, upon continued reduction in fares for both inbound and outbound transport services as well as further fare concessions from some of the public transport operators. This followed a 0.6% decline in the second quarter. The charges for miscellaneous services fell by 3.7% in both quarters, with charges for package tours and for telephone and other communications services showing the most visible drop. The prices of alcoholic drinks and tobacco were virtually unchanged in the third quarter,

/having

having edged up by 0.2% in the second quarter. The charges for electricity, gas and water were only slightly higher by 0.1% in the third quarter, after a 7.6% surge in the second quarter⁽³⁾. This mainly reflected the dampening effect brought about by the waiver of water and sewage charges for August - November. On housing, the cost of private dwellings had a larger decrease in the third quarter than in the second quarter, by 9.5% as against 4.9%. Besides the further softening in flat rentals⁽⁴⁾, private housing cost was also brought down by the rates concession for July - September. Yet the cost of public dwellings, though still up by 1.5% in the third quarter, had a much lesser increase than that of 11.8% in the second quarter. The surge in the second quarter was due to a low base of comparison brought about by the rates concession granted last year, which had a more profound effect on public housing cost. Meanwhile, the prices of durable goods exhibited a narrowed decrease, from 7.7% in the second quarter to 6.7% in the third quarter, mainly attributable to more modest reductions in the prices of certain household appliances, travel and sports goods, and computers and telecommunications equipment. The prices of clothing and footwear also showed a milder decline, from 6.3% in the second quarter to 2.8% in the third quarter, on account of a smaller fall in the prices of outerclothing and men's footwear. As to the prices of miscellaneous goods, there was a faster increase by 1.6% in the third quarter, as compared to a 0.5% rise in the second quarter. This was largely due to higher prices of jewellery, along with the pick-up in gold prices in recent months.

6.6 For the first nine months of 2003 as a whole, the prices of durable goods, private housing cost, and prices of clothing and footwear had more distinct decreases, by 6.8%, 5.9% and 4.2% respectively from a year earlier. By comparison, the charges for miscellaneous services, prices of basic foodstuffs, charges for meals at restaurants, and cost of transport fell to a lesser extent, by 3.0%, 1.8%, 1.6% and 0.5% respectively. On the other hand, the prices of alcoholic drinks and tobacco, charges for electricity, gas and water, and prices of miscellaneous goods moved up, albeit only modestly, by 0.2%, 0.5% and 1.8% respectively. Public housing cost rose considerably more, by 8.3%. But this was due to a low base of comparison brought about by the rates concession granted last year.

/Table 6.3

Table 6.3

**Consumer Price Indices by component
(year-on-year rate of change (%))**

(a) In the second and third quarters of 2003

Expenditure component	Composite CPI		CPI(A)		CPI(B)		CPI(C)	
	2003 Q2	2003 Q3	2003 Q2	2003 Q3	2003 Q2	2003 Q3	2003 Q2	2003 Q3
Food	-1.5	-1.5	-1.6	-1.5	-1.7	-1.6	-0.8	-1.6
<i>Meals bought away from home</i>	-1.6	-1.6	-1.7	-1.3	-1.9	-1.5	-0.8	-2.0
<i>Other foodstuffs</i>	-1.3	-1.5	-1.5	-1.8	-1.4	-1.6	-0.8	-0.7
Housing ^(a)	-3.4	-7.9	-1.6	-6.6	-3.7	-8.1	-5.1	-9.1
<i>Private dwellings</i>	-4.9	-9.5	-4.6	-9.1	-4.6	-9.3	-5.4	-10.2
<i>Public dwellings</i>	11.8	1.5	11.8	1.5	11.9	1.5	NA	NA
Electricity, gas and water	7.6	0.1	8.4	0.1	7.4	0.1	6.6	0.4
Alcoholic drinks and tobacco	0.2	*	0.2	-0.1	0.2	-0.1	0.8	0.4
Clothing and footwear	-6.3	-2.8	-5.5	-3.2	-5.5	-2.9	-8.4	-2.1
Durable goods	-7.7	-6.7	-7.6	-6.5	-7.9	-6.8	-7.4	-6.8
Miscellaneous goods	0.5	1.6	0.1	0.7	0.5	1.5	1.0	2.5
Transport	-0.6	-0.8	-1.3	-1.3	-0.8	-0.9	0.4	-0.3
Miscellaneous services	-3.7	-3.7	-4.3	-4.1	-3.4	-3.4	-3.6	-3.9
All items	-2.5	-3.6	-1.8	-3.3	-2.6	-3.7	-2.9	-4.1

(b) In 2002 and the first nine months of 2003

Expenditure component	Composite CPI		CPI(A)		CPI(B)		CPI(C)	
	2002	2003 Jan-Sep	2002	2003 Jan-Sep	2002	2003 Jan-Sep	2002	2003 Jan-Sep
Food	-2.1	-1.6	-2.2	-1.8	-2.1	-1.8	-1.7	-1.1
<i>Meals bought away from home</i>	-1.5	-1.6	-1.7	-1.6	-1.9	-1.8	-0.3	-1.0
<i>Other foodstuffs</i>	-3.1	-1.8	-2.9	-2.0	-2.6	-1.8	-4.0	-1.4
Housing ^(a)	-5.7	-4.5	-5.7	-2.9	-5.9	-4.7	-5.5	-6.0
<i>Private dwellings</i>	-6.5	-5.9	-6.8	-5.7	-6.6	-5.7	-6.0	-6.5
<i>Public dwellings</i>	-2.7	8.3	-2.7	8.3	-2.7	8.4	NA	NA
Electricity, gas and water	-7.0	0.5	-8.2	0.2	-6.7	0.6	-5.1	0.9
Alcoholic drinks and tobacco	2.4	0.2	2.4	0.1	2.4	0.2	2.2	0.9
Clothing and footwear	0.7	-4.2	2.6	-4.1	2.0	-3.9	-2.8	-4.9
Durable goods	-6.3	-6.8	-6.0	-6.8	-6.5	-7.0	-6.2	-6.6
Miscellaneous goods	1.7	1.8	1.0	0.8	1.4	1.7	2.8	2.9
Transport	-0.6	-0.5	-0.6	-1.1	-0.5	-0.6	-0.9	0.2
Miscellaneous services	-2.3	-3.0	-3.3	-3.6	-2.3	-2.8	-1.4	-2.8
All items	-3.0	-2.7	-3.2	-2.3	-3.1	-2.8	-2.8	-2.9

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.

(*) Change of less than 0.05%.

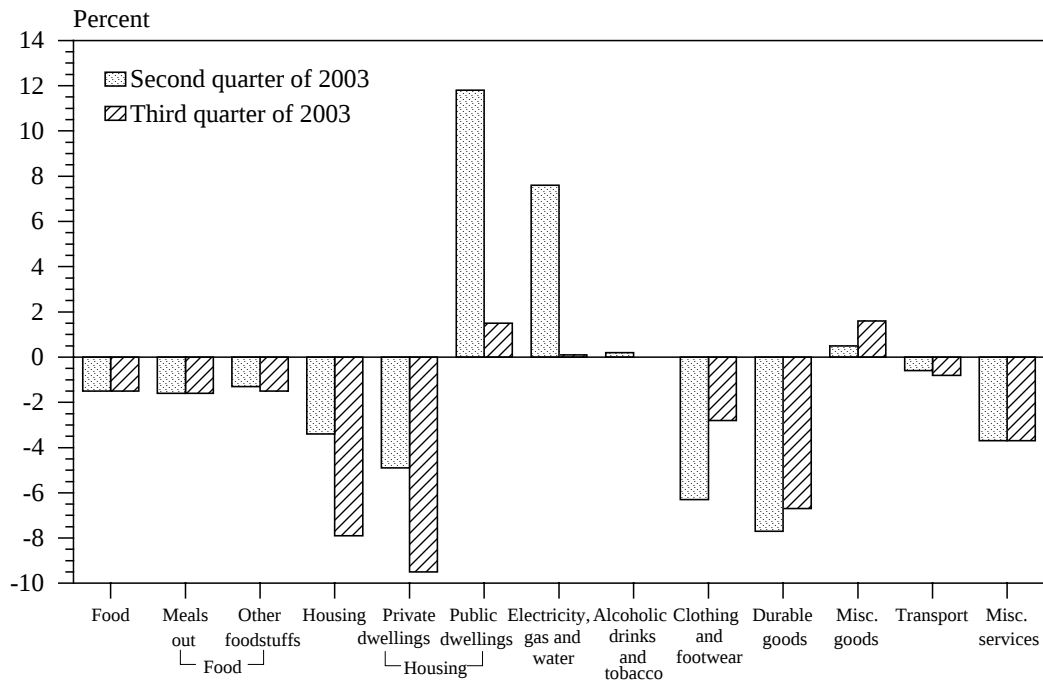
NA Not applicable.

/Diagram 6.4

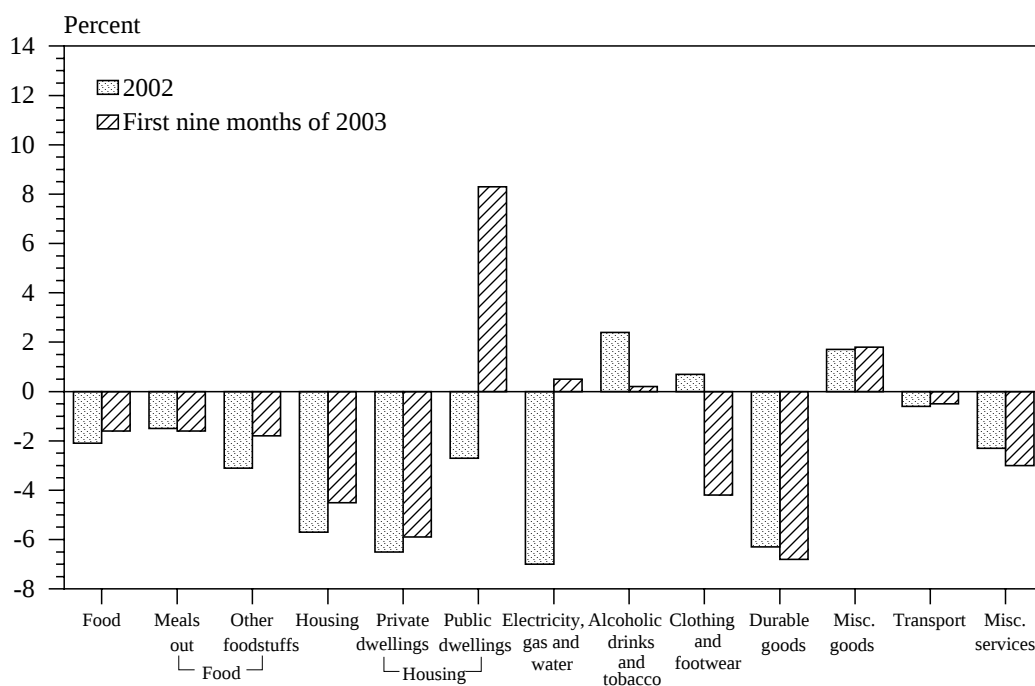
Diagram 6.4

**Composite Consumer Price Index by component
(year-on-year rate of change)**

(a) In the second and third quarters of 2003



(b) In 2002 and the first nine months of 2003

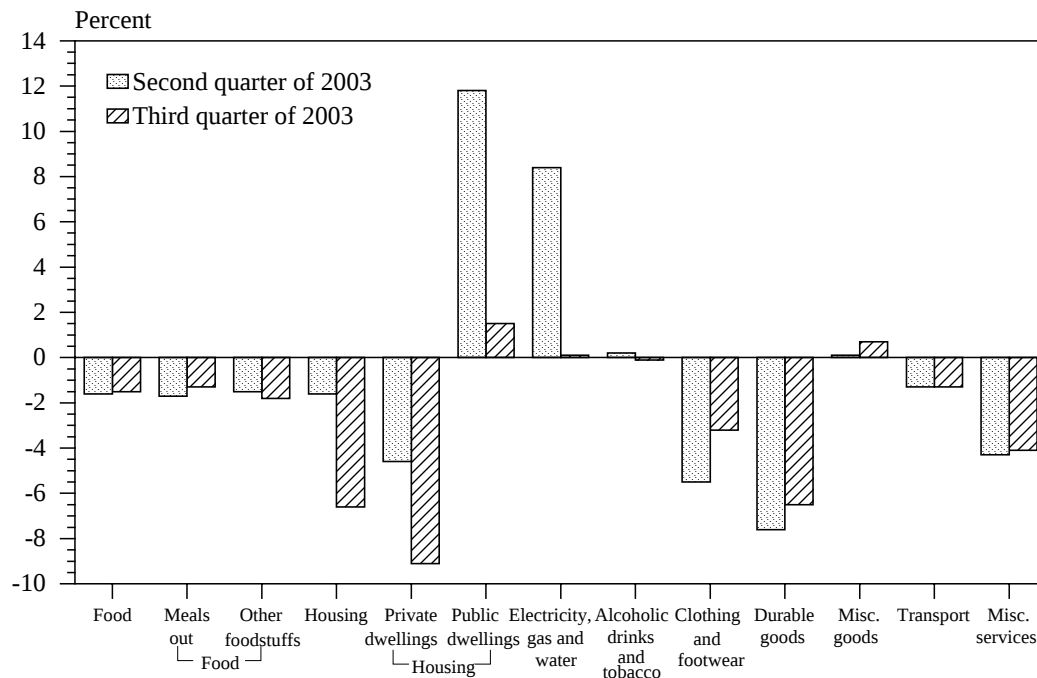


/Diagram 6.5

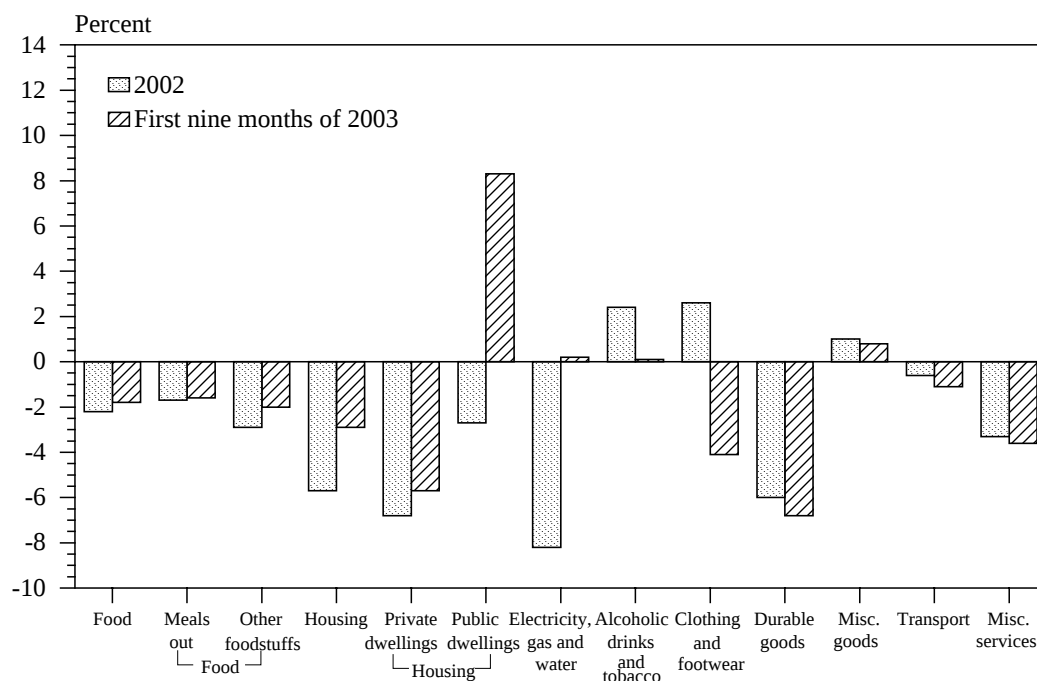
Diagram 6.5

**Consumer Price Index (A) by component
(year-on-year rate of change)**

(a) In the second and third quarters of 2003



(b) In 2002 and the first nine months of 2003



/Box 6.1

Box 6.1

Impact of the Government's special relief measures on the Consumer Price Indices

The analysis below covers those special relief measures granted by the Government since 1998, including mainly rates rebate, waiver of public housing rentals, and waiver of water and sewage charges, which have a direct impact on the CPI.

In 1998 and 1999, the Government granted a rates rebate to households, to help them tide over the economic difficulties brought about by the Asian financial crisis. This had the effect of lowering the Composite CPI by 0.4 and 0.2 of a percentage point respectively in those two years. In 2001, public housing rentals were waived for the month of December. Consequently, the Composite CPI was dampened by 0.2 of a percentage point in that year. In 2002, further relief measures, including a rates rebate and a waiver of water and sewage charges, were implemented. These pulled down the Composite CPI by 1.1 percentage points in that year.

The special relief measures accorded so far in this year were intended to alleviate the adverse impact of SARS. The measures relevant to the CPI comprised mainly a rates rebate for the third quarter of 2003 up to a maximum of \$1,250 per tenement, and a waiver of water and sewage charges for August - November 2003 with respective caps at \$267 and \$67 per domestic household. These measures taken together were estimated to dampen the Composite CPI by around 0.3 of a percentage point for the whole year.

Impact of the Government's special relief measures on the Composite CPI

Of which:

	Year-on-year change in <u>the Composite CPI</u> (%)	Attributed to the Government's <u>special relief measures</u> (% points)
1998	2.8	-0.4
1999	-4.0	-0.2
2000	-3.8	NA
2001	-1.6	-0.2
2002	-3.0	-1.1
2003	-2.7*	-0.4 [#]

Notes : (*) Broad forecast for the year.

(#) Including also the residual impact of the waiver of water and sewage charges granted for the financial year April 2002 - March 2003.

NA Not applicable.

Also noteworthy is the fact that, since Government fees and charges constitute a larger share in the total expenditure of lower to middle income households, as against the share in the total expenditure of higher income household, the special relief measures tend to affect the CPI(A) and CPI(B) more than the CPI(C). Taking the waiver of public housing rentals for the month of December 2001 as an example, this measure has lowered both the CPI(A) and CPI(B) in the respective period, but has had no effect on the CPI(C) where public housing rentals carry zero weighting.

/Import

Import prices

6.7 The *prices of imports of goods*, as measured by the unit value index of imports of goods, declined by 0.9% in the third quarter of 2003 over a year earlier, following a 0.3% fall in the second quarter. For the first nine months of 2003 as a whole, the prices of imports of goods were 0.4% lower than a year earlier, considerably narrowed from the 3.9% drop in 2002. This was attributable to a weakening in the US dollar and higher world commodity prices, including oil prices, over the past year or so.

6.8 Analysed by major *source*, the prices of goods imported from Taiwan and the United States went down by 1.3% and 1.1% respectively in the third quarter of 2003 from a year earlier, having fallen by 0.3% and 1.4% in the second quarter. The prices of goods imported from the Mainland fell only slightly, by 0.1% in the third quarter of 2003 over a year earlier, after edging up by 0.1% in the second quarter. For this source, the increases in the prices of consumer goods, raw materials and semi-manufactures, and fuels virtually offset the decreases in the prices of capital goods and foodstuffs. On the other hand, the prices of goods imported from Japan continued to move up, by 0.9% in the third quarter of 2003 over a year earlier, further to a 2.9% increase in the second quarter. The strengthening of the Japanese yen against the US dollar and hence the Hong Kong dollar was the major contributory factor.

/Table 6.4

**World commodity prices
(year-on-year rate of change (%))**

Source : IMF International Financial Statistics.

Spot price of crude oil*



227

Table 6.5

**Unit value indices of imports of goods by major source
(year-on-year rate of change (%))**

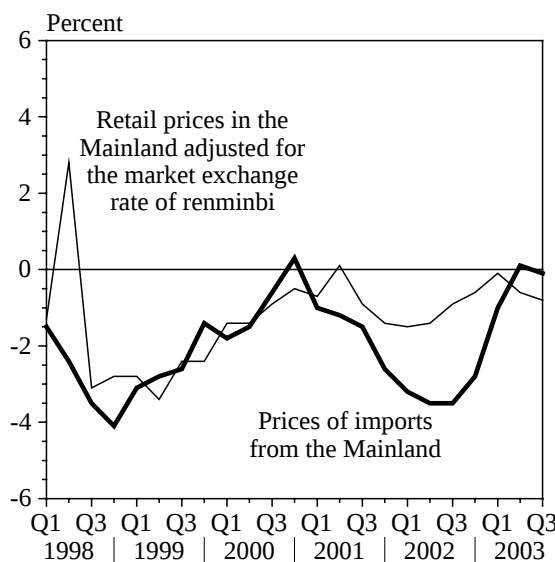
		<u>Mainland of China</u>	<u>Japan</u>	<u>Taiwan</u>	<u>United States</u>	<u>All sources</u>
2002	Annual	-3.3	-3.7	-3.5	-5.0	-3.9
	H1	-3.4	-6.1	-5.4	-5.3	-4.8
	H2	-3.2	-1.3	-1.7	-4.6	-3.0
	Q1	-3.2	-7.0	-6.4	-5.1	-4.9
	Q2	-3.5	-5.4	-4.4	-5.6	-4.6
	Q3	-3.5	-2.1	-2.7	-4.6	-3.6
	Q4	-2.8	-0.5	-0.6	-4.5	-2.3
2003	H1	-0.4	3.1	0.3	-2.0	-0.2
	Q1-Q3	-0.3	2.3	-0.3	-1.6	-0.4
	Q1	-1.0	3.3	1.1	-2.6	-0.1
	Q2	0.1	2.9	-0.3	-1.4	-0.3
	Q3	-0.1	0.9	-1.3	-1.1	-0.9

/Diagram 6.7

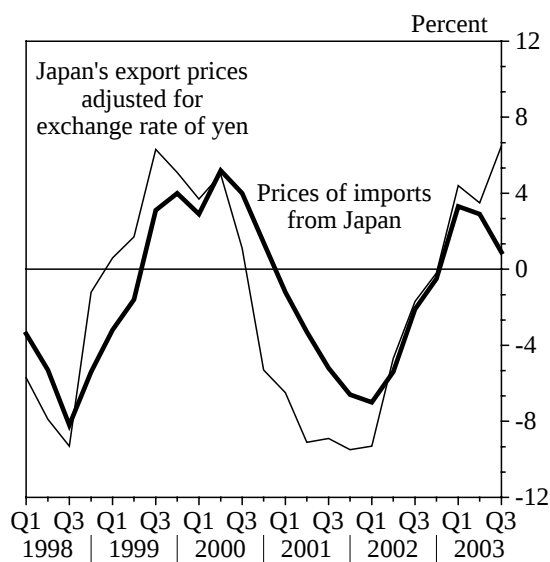
Diagram 6.7

**Prices of imports of goods by major source
(year-on-year rate of change)**

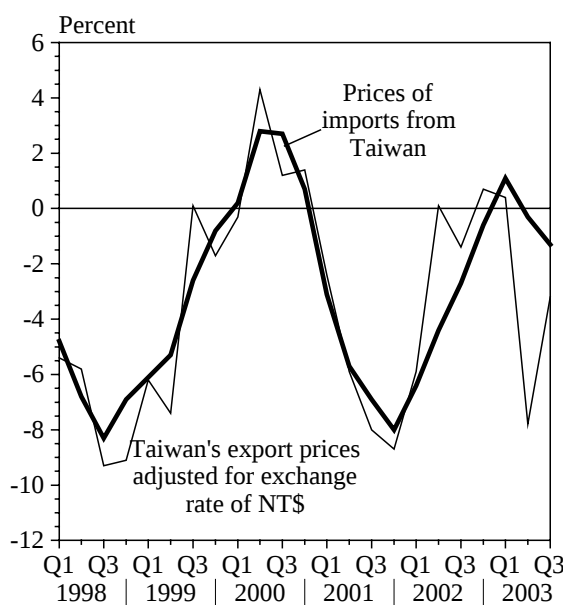
**(a) For imports from the
mainland of China**



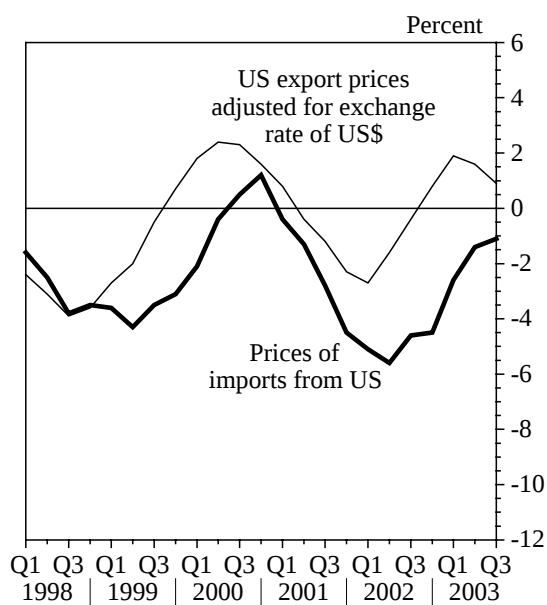
(b) For imports from Japan



(c) For imports from Taiwan



(d) For imports from the United States



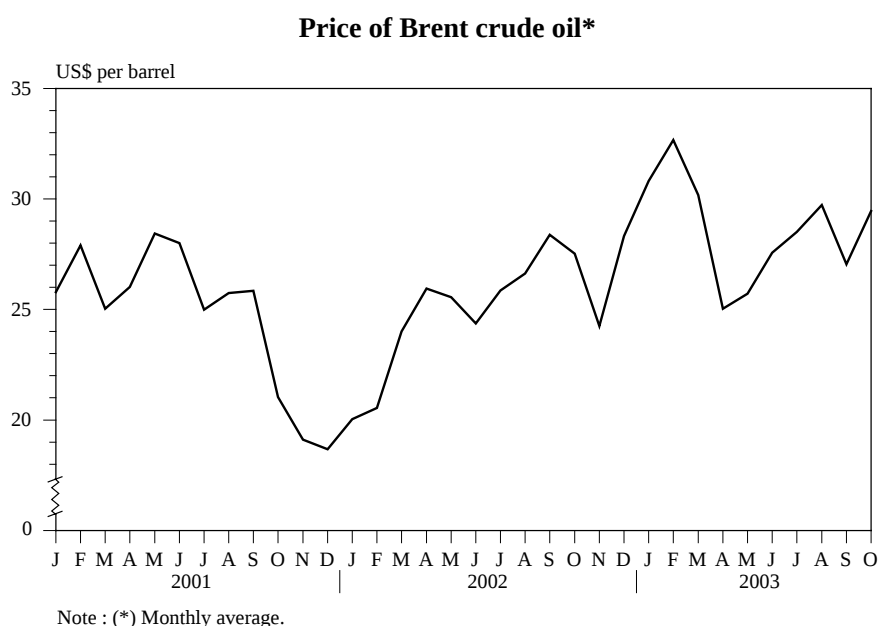
/Box 6.2

Box 6.2

Recent trend in international crude oil prices

Over the past two years, international crude oil prices have been generally on a rising trend. The price of Brent crude oil picked up from a low of around US\$18 per barrel in late 2001 to over US\$30 per barrel in early 2003, and stayed at around US\$28-30 per barrel in the more recent months.

While market fundamentals, such as the demand and supply balance, the level of oil inventories, and OPEC's production situation, played an important role in influencing crude oil prices, major geo-political events and developments, including in particular the 911 incident in the United States in September 2001 and the US-led war on Iraq in March 2003, had led to added volatilities in crude oil prices.



More specifically, the 911 incident in September 2001 had triggered off a sharp plunge in crude oil prices. Market sentiment was pummeled by heightened alert to global terrorism, with consequential down-drag on the global economy and hence on oil demand. The price of Brent plummeted to a low of US\$17.2 per barrel on 15 November 2001, before rebounding somewhat to around US\$20 per barrel in early 2002 following the output cut by both OPEC and major non-OPEC producers.

Crude oil prices bounced back noticeably during the course of 2002 amidst heightened political tensions in the Middle East, as conflict between Israel and Palestine intensified, and as the possibility of war on Iraq grew. Tightened oil supply due to OPEC's output cut and increased demand due to replenishment of US oil inventories also rendered support to firmer oil prices. At end-2002, the price of Brent rose to around US\$30 per barrel.

In early 2003, crude oil prices surged further, in face of the imminent outbreak of war on Iraq and the supply disruption caused by the strike in Venezuela. The price of Brent soared to a 2-year high of US\$34.5 per barrel on 6 March 2003. Upon the quick ending of the war on Iraq, the market refocused on the demand-supply fundamentals. The slow recovery of oil production in Iraq and the low level of global oil inventories, against strengthening oil demand amidst the global economic recovery, held up oil prices. In late 2003, the price of Brent stayed firm at around \$28-30 per barrel.

6.9 The *prices of retained imports*, as measured by the unit value index of retained imports, were 2.7% higher in the third quarter of 2003 than a year earlier, further to a 2.8% rise in the second quarter. For the first nine months of 2003 as a whole, there was an increase of 2.5%, reversing the 9.7% dip in 2002. Yet the effect of the recent pick-up in prices of retained imports on local consumer prices was still not generally apparent so far.

6.10 Analysed by *end-use category* and on a year-on-year comparison, the prices of retained imports of fuels were lifted by 6.9% in the third quarter of 2003, albeit lesser than the 8.9% increase in the second quarter. A firming up in international crude oil prices more recently, amidst concern about the relatively low level of oil inventories, was a major contributory factor. The prices of retained imports of raw materials and semi-manufactures had a steeper rise, by 7.7% in the third quarter, as against 4.0% in the second quarter. There were accelerated increases in the import prices of base metals (other than iron and steel), leather skin, and wood and lumber. The prices of retained imports of consumer goods went up by 6.0% in the third quarter, moderated from the 7.2% hike in the second quarter. To some extent, this was influenced by lesser increases in the import prices of passenger cars as well as watches and clocks. The prices of retained imports of foodstuffs rose by 1.0% in the third quarter, likewise narrowed from the 1.3% rise in the second quarter. This was partly attributable to enlarged decreases in the import prices of vegetables, tea and coffee, which helped cushion increases in the import prices of rice, cooking oil and live poultry. On the other hand, the prices of retained imports of capital goods dropped further, by 8.5% in the third quarter of 2003, having dipped by 5.1% in the second quarter. Larger declines in the import prices of telecommunications equipment, computer equipment, office machinery and electrical machinery contributed.

/Table 6.6

Table 6.6

**Unit value indices of retained imports by end-use category
(year-on-year rate of change (%))**

		<u>Food- stuffs</u>	<u>Consumer goods</u>	<u>Fuels</u>	<u>Raw materials and semi- manufactures</u>	<u>Capital goods</u>	<u>All categories</u>
2002	Annual	-4.1	-9.5	0.5	-9.5	-11.4	-9.7
	H1	-5.9	-9.6	-10.7	-12.4	-11.8	-11.7
	H2	-2.4	-9.4	11.8	-6.2	-10.9	-7.6
	Q1	-6.0	-9.6	-15.7	-12.0	-11.0	-11.6
	Q2	-5.8	-9.5	-6.9	-12.6	-12.7	-11.7
	Q3	-3.2	-9.5	0.1	-9.5	-11.4	-9.6
	Q4	-1.6	-9.3	25.6	-2.5	-10.2	-5.5
2003	H1	0.5	4.8	21.5	3.3	-5.5	2.4
	Q1-Q3	0.7	5.2	15.9	4.8	-6.6	2.5
	Q1	-0.2	2.1	37.3	2.3	-6.1	1.9
	Q2	1.3	7.2	8.9	4.0	-5.1	2.8
	Q3	1.0	6.0	6.9	7.7	-8.5	2.7

/Prices

Prices of key inputs

6.11 On *labour cost*, overall wages and earnings were both down by 2.5% in money terms in mid-2003 from a year earlier, amidst the still slack labour market conditions. On *property cost*, the prices of office space, shopping space and conventional flatted factory space all dropped, by an average of 14.1%, 3.9% and 8.2% respectively in the third quarter of 2003 from a year earlier, as did their rentals, by an average of 16.2%, 10.3% and 12.3% respectively. On *capital equipment and material costs*, the prices of retained imports of capital goods were lower by 6.6% in the first nine months of 2003 than a year earlier, although the prices of retained imports of raw materials and semi-manufactures were higher by 4.8%. Thus in overall terms, the cost of doing business should have gone down further.

Prices of local manufacturing output

6.12 The *prices of local manufacturing output*, as measured by the Producer Price Index⁽⁵⁾, continued on a downtrend. Comparing the second quarter of 2003 with a year earlier, there was a decrease of 1.0%. This was broadly similar to the 1.2% decline in the first quarter. For the first half of 2003 as a whole, the fall was 1.1%, which was nevertheless smaller than the 2.7% drop in 2002. Analysed by major *industry group* and on a year-on-year comparison, output prices in fabricated metal products fell more visibly, by 4.1% in the second quarter of 2003. This was followed by output prices in paper products and printing (down by 2.4%), consumer electrical and electronic products (1.4%), machinery and equipment (0.6%), and textiles (0.3%). On the other hand, output prices in plastic products and in wearing apparel rose by 2.6% and 0.2% respectively.

/Table 6.7

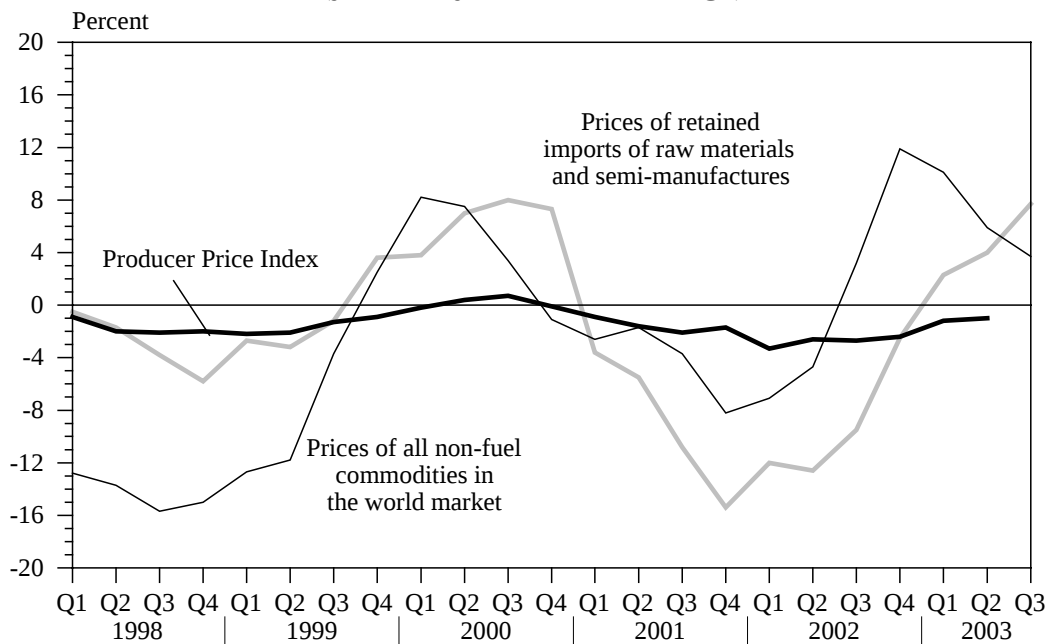
Table 6.7

**Producer Price Index for the local manufacturing sector
(year-on-year rate of change (%))**

<u>Industry group</u>	<u>2002</u>					<u>2003</u>	
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
Wearing apparel	-3.5	-3.2	-4.1	-3.6	-2.9	-0.8	0.2
Textiles	-1.4	-1.8	-1.8	-1.1	-0.7	-0.6	-0.3
Plastic products	-2.7	-1.7	-1.5	-4.1	-3.7	0.1	2.6
Consumer electrical and electronic products	-4.7	-4.4	-5.7	-4.5	-4.2	-1.7	-1.4
Machinery and equipment	-5.1	-3.8	-5.2	-5.5	-5.9	-3.1	-0.6
Fabricated metal products	-2.6	-3.1	-2.5	-2.0	-2.6	-3.0	-4.1
Paper products and printing	-2.4	-2.6	-1.7	-2.0	-3.2	-2.0	-2.4
Overall manufacturing	-2.7	-3.3	-2.6	-2.7	-2.4	-1.2	-1.0

Diagram 6.8

**Producer Price Index, world commodity prices, and prices
of retained imports of raw materials and semi-manufactures
(year-on-year rate of change)**



/Prices

Prices of output in selected service sectors

6.13 The *prices of output in selected service sectors*, as measured by the respective Producer Price Indices, exhibited quite a broad-based decline in the second quarter. Specifically, output prices in telecommunications plummeted by 12.0% in the second quarter of 2003 over a year earlier. This was mainly because the charges for mobile phone services, international calls and Internet services all continued to drift lower, amidst keen competition in the market. Lower prices of mobile phone sets and related items also contributed. Output prices in hotels and boarding houses were reduced by 10.6%, attributable to a slash in room tariffs after the outbreak of SARS. Output prices in land transport went down by 2.3%, reflecting lower hiring charges for taxis upon the impact of SARS. Output prices in air transport fell by 0.6%, as a reduction in the fares for air passenger transport offset an elevation in the charges for air cargo forwarding services. On the other hand, output prices in maritime transport rose by 7.5%. This was bolstered in part by increased demand for sea cargo forwarding services, along with continued expansion in external trade. Output prices in miscellaneous communications services went up by 7.0%, on account of upward adjustment in the charges for international courier services.

/Table 6.8

Table 6.8

Producer Price Indices for selected service sectors^(a)
(year-on-year rate of change (%))

	<u>2002</u>					<u>2003</u>	
	<u>Annual</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>
<u>Selected service sector</u>							
Hotels and boarding houses	-1.1	-5.8	-4.2	-3.6	9.3	1.6	-10.6
Land transport	-1.9	-1.4	-2.0	-2.1	-2.1	-0.7	-2.3
Maritime transport	-3.0	-9.4	-5.5	2.9	0.9	5.5	7.5
Air transport	0.3	-5.5	-3.4	3.4	7.1	1.8	-0.6
Telecommunications	-18.6	-21.7	-24.5	-15.5	-11.0	-7.7	-12.0
Miscellaneous communications services	3.9	0.4	0.1	5.1	9.8	7.1	7.0

Note : (a) Producer Price Indices for other service sectors are not available, due to the difficulties involved in defining and delineating the various types of services and hence in measuring their respective price changes. This is particularly so for such sectors as banking and insurance, where the producers often do not charge their customers explicitly.

Export prices

6.14 The *prices of total exports of goods*, as measured by the unit value index of total exports of goods, were lowered by 1.8% in the third quarter of 2003 over a year earlier, exceeding the 1.4% drop in the second quarter. For the first nine months of 2003 as a whole, the decline in the prices of total exports of goods, by 1.4% over a year earlier, was nevertheless smaller than that of 2.7% in 2002. Within the total, the prices of domestic exports rose by 0.6% in the first nine months of 2003 over a year earlier, while the prices of re-exports fell by 1.6%.

/6.15

6.15 Analysed by major *market* and on a year-on-year comparison, the prices of total exports of goods fell across-the-board. Specifically, the prices of total exports of goods to Singapore declined by 4.5% in the third quarter of 2003, after a 3.1% fall in the second quarter. The enlarged decrease was attributable in part to an accentuated decline in the prices of capital goods, such as office machines, exported to this market. The prices of total exports of goods to the United Kingdom, Japan and the Mainland went down by 2.1%, 2.1% and 1.7% respectively in the third quarter, again exceeding the decreases of 1.7%, 1.2% and 1.0% in the second quarter. Larger reductions in the prices of raw materials and semi-manufactures and of capital goods exported to these markets were the major contributory factor. The prices of total exports of goods to Germany eased by 2.9% in both the second and third quarters, with an enlarged dip in the prices of capital goods offsetting a moderated decline in the prices of raw materials and semi-manufactures. As to the prices of total exports of goods to the United States, the decrease tapered from 0.6% to 0.3% between the two quarters, on account of lesser decreases in the prices of consumer goods and of capital goods to this market.

Table 6.9

**Unit value indices of total exports of goods by major market
(year-on-year rate of change (%))**

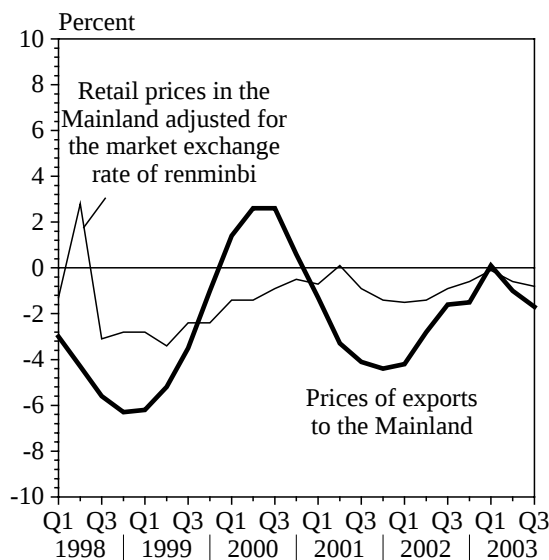
		<u>United States</u>	<u>Mainland of China</u>	<u>Germany</u>	<u>United Kingdom</u>	<u>Japan</u>	<u>Singapore</u>	<u>All markets</u>
2002	Annual	-2.6	-2.5	-3.2	-2.5	-3.2	-3.9	-2.7
	H1	-2.2	-3.5	-3.4	-3.0	-3.5	-4.2	-3.1
	H2	-2.9	-1.6	-2.9	-2.1	-2.9	-3.4	-2.4
	Q1	-1.9	-4.2	-4.0	-3.6	-3.5	-4.8	-3.4
	Q2	-2.4	-2.8	-2.8	-2.3	-3.4	-3.5	-2.7
	Q3	-3.2	-1.6	-2.8	-2.3	-2.7	-3.1	-2.4
	Q4	-2.6	-1.5	-3.0	-1.9	-3.0	-3.6	-2.3
2003	H1	-0.9	-0.5	-2.6	-1.4	-1.1	-2.4	-1.1
	Q1-Q3	-0.6	-1.0	-2.7	-1.7	-1.5	-3.2	-1.4
	Q1	-1.3	0.1	-2.3	-1.0	-1.1	-1.6	-0.9
	Q2	-0.6	-1.0	-2.9	-1.7	-1.2	-3.1	-1.4
	Q3	-0.3	-1.7	-2.9	-2.1	-2.1	-4.5	-1.8

/Diagram 6.9

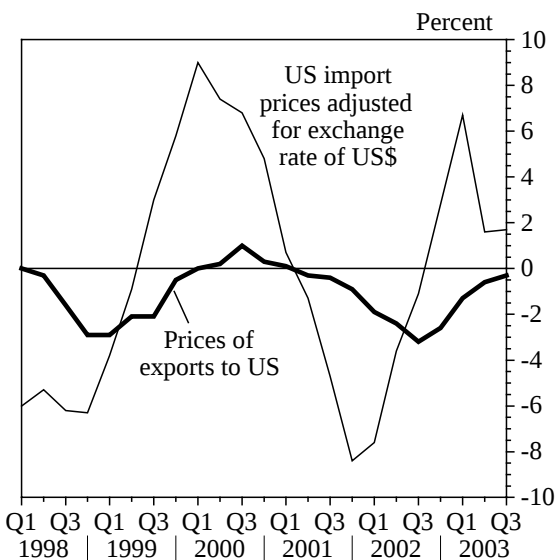
Diagram 6.9

**Prices of total exports of goods by major market
(year-on-year rate of change)**

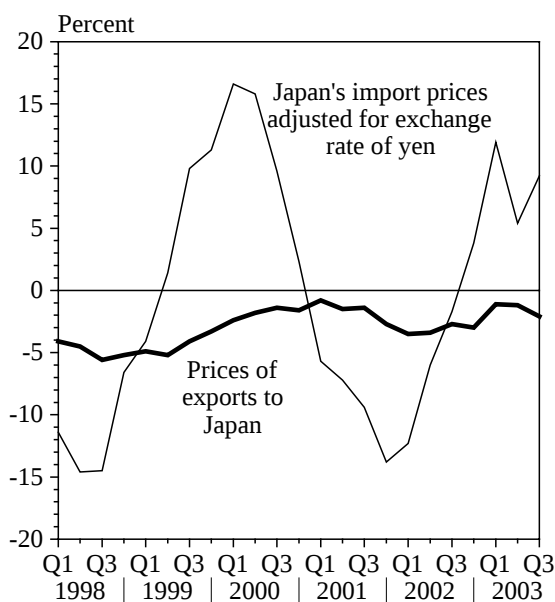
**(a) For exports to the
mainland of China**



(b) For exports to the United States



(c) For exports to Japan



(d) For exports to Germany



/Terms

Terms of trade

6.16 With the prices of total exports of goods falling to a larger extent than the prices of imports of goods, the *terms of trade in goods*⁽⁶⁾ for Hong Kong moved down by 0.9% in the third quarter of 2003 over a year earlier. This compared with a 1.1% fall in the second quarter. For the first nine months of 2003 as a whole, there was also a 0.9% decrease, which contrasted with a 1.2% rise in 2002.

Table 6.10

Terms of trade in goods

		Index on the terms of trade in goods (2000 = 100)	Year-on-year rate of change (%)
2002	Annual	102.1	1.2
	H1	102.3	1.8
	H2	101.9	0.7
	Q1	102.2	1.6
	Q2	102.5	2.0
	Q3	102.1	1.2
	Q4	101.7	*
2003	H1	101.4	-1.0
	Q1-Q3	101.3	-0.9
	Q1	101.4	-0.8
	Q2	101.3	-1.1
	Q3	101.1	-0.9

Note : (*) Change of less than 0.05%.

/Diagram 6.10

Diagram 6.10

**Unit value indices of total exports of goods and imports of goods
(year-on-year rate of change)**

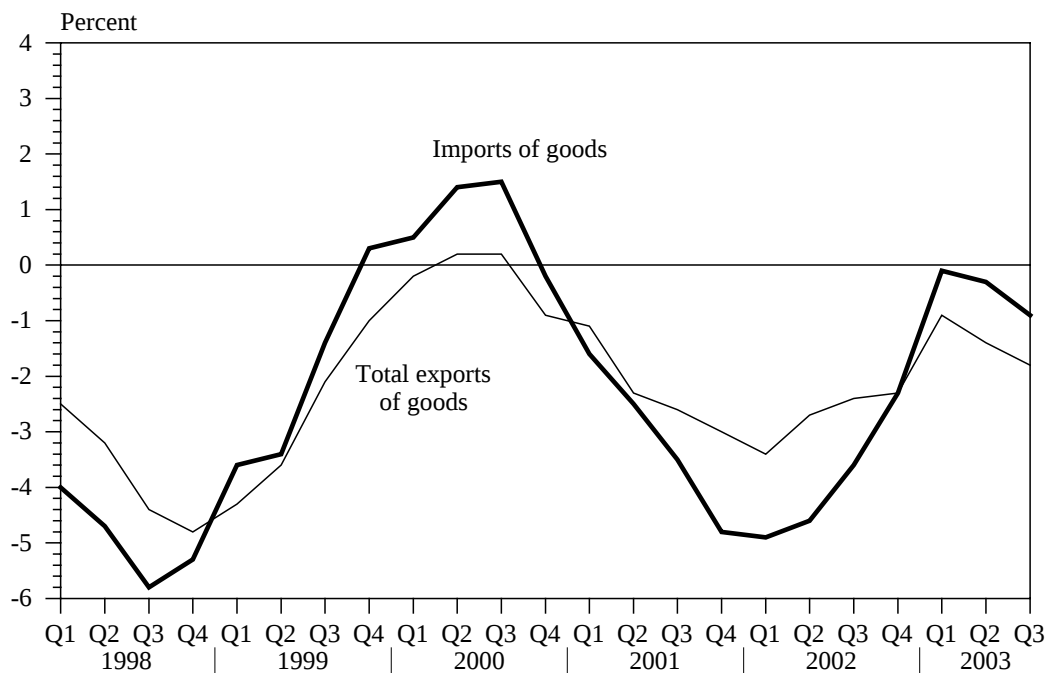
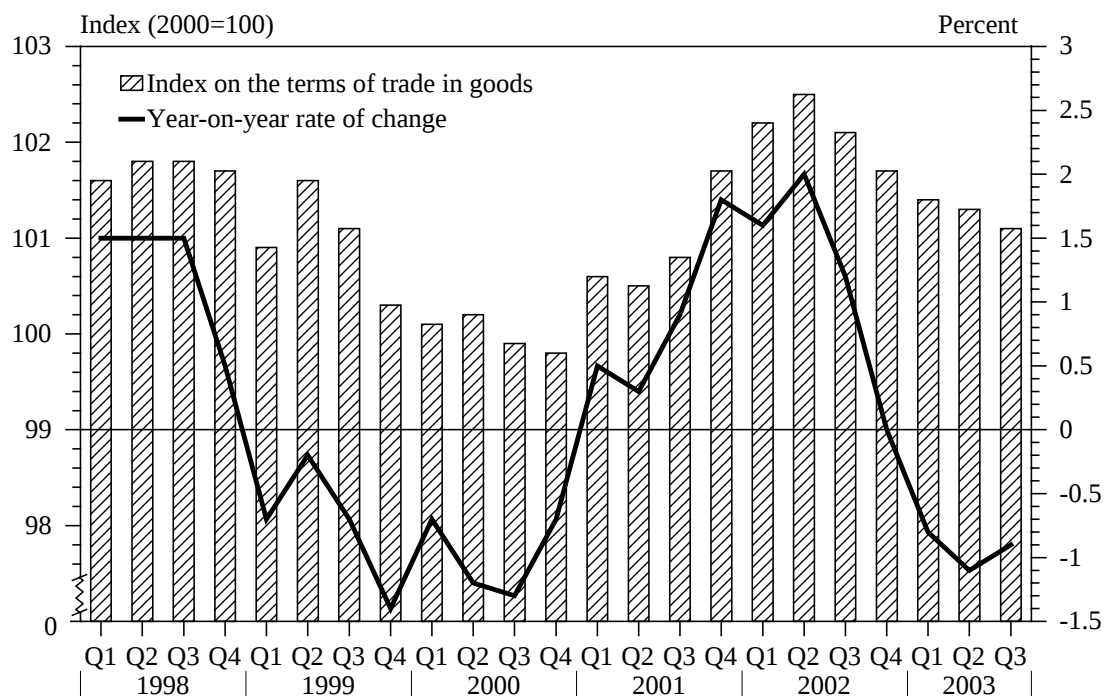


Diagram 6.11

Terms of trade in goods



/GDP

GDP deflator

6.17 The *GDP deflator*⁽⁷⁾, as a broad measure of overall price change in the economy, declined by 5.7% in the third quarter of 2003 over a year earlier, even larger than the 5.4% fall in the second quarter. This was mainly due to enlarged declines in the price deflator for private consumption expenditure and for gross domestic fixed capital formation, more than offsetting lesser deterioration in the terms of trade in goods and in services. Within the GDP deflator, the *domestic demand deflator* and the *total final demand deflator* both had enlarged declines, by 4.5% and 3.1% respectively in the third quarter of 2003 over a year earlier as against 4.1% and 2.8% in the second quarter. On a seasonally adjusted quarter-to-quarter comparison, the GDP deflator fell by 1.2% in the third quarter of 2003, which was nevertheless smaller than the 1.6% decrease in the second quarter.

/Table 6.11

Table 6.11

**GDP deflator and the main expenditure component deflators
(year-on-year rate of change (%))**

	<u>2001[#]</u>	<u>2002[#]</u>	<u>2002</u>				<u>2003</u>		
			<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3[#]</u>	<u>Q4[#]</u>	<u>Q1[#]</u>	<u>Q2[#]</u>	<u>Q3⁺</u>
Private consumption expenditure	-1.3	-3.6	-3.0	-3.6	-4.0	-4.1	-2.6	-3.4	-3.8
Government consumption expenditure	1.1	-0.5	1.4	-0.6	-0.7	-2.6	-2.5	-3.6	-3.5
Gross domestic fixed capital formation	-6.6	-8.1	-7.4	-8.5	-9.2	-7.5	-6.8	-6.0	-7.2
Total exports of goods	-2.6	-2.9	-3.8	-3.0	-2.7	-2.4	-1.3	-1.8	-2.3
Imports of goods	-3.5	-4.2	-5.2	-4.9	-3.9	-2.6	-0.8	-0.8	-1.6
Exports of services	-4.0	-2.1	-5.0	-2.7	-0.5	-0.5	-0.9	-3.0	-2.1
Imports of services	-1.5	0.2	-2.4	*	1.4	2.0	3.4	1.6	1.2
Gross Domestic Product	-1.9	-3.0	-2.3 <-0.7>	-2.2 <-0.8>	-3.1 <-0.9>	-4.1 <-1.6>	-4.6 <-1.4>	-5.4 <-1.6>	-5.7 <-1.2>
Total final demand	-2.7	-3.5	-3.9	-3.6	-3.3	-3.1	-2.1	-2.8	-3.1
Domestic demand	-2.5	-4.5	-3.5	-4.5	-5.1	-5.0	-3.8	-4.1	-4.5

Notes : (#) Revised figures.

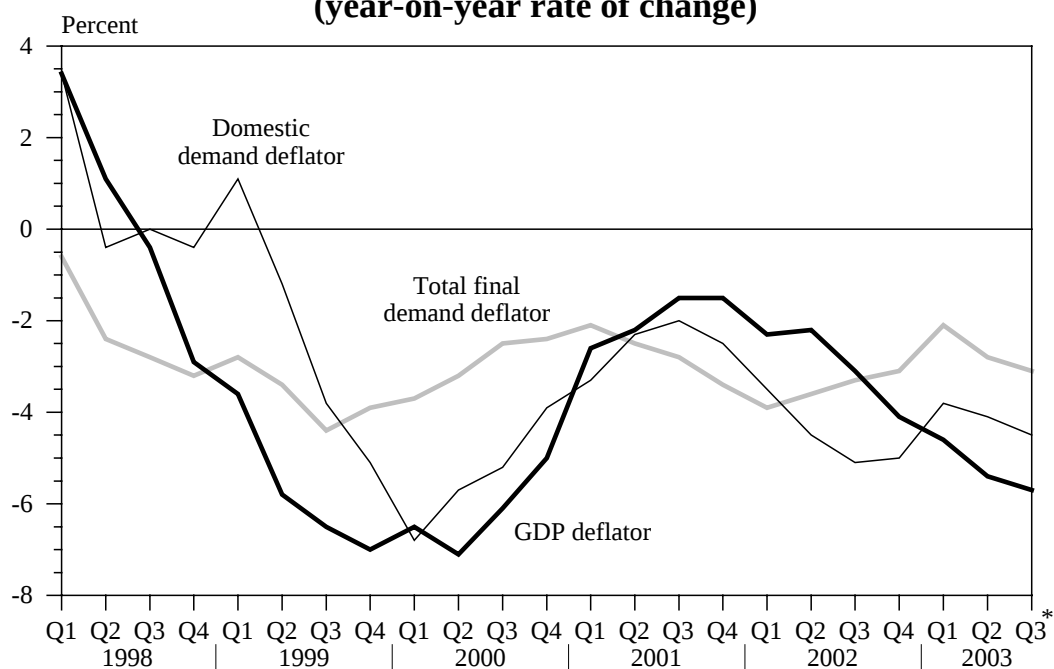
(+) Preliminary figures.

< > Seasonally adjusted quarter-to-quarter % change.

(*) Change of less than 0.05%.

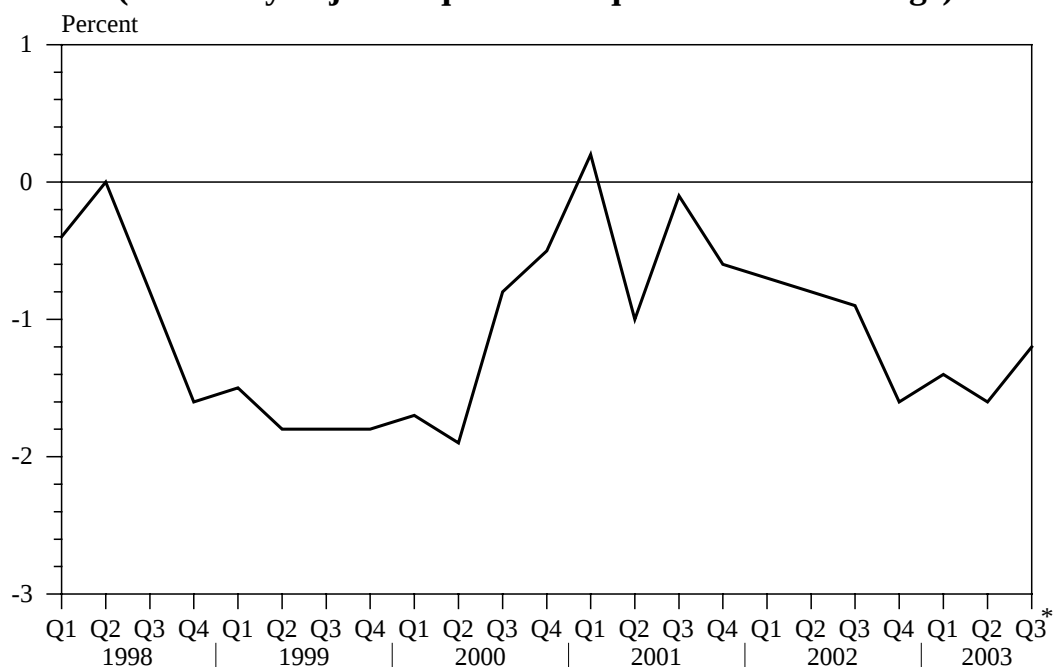
/Diagram 6.12

Diagram 6.12
GDP deflator, total final demand deflator
and domestic demand deflator
(year-on-year rate of change)



Note : (*) Preliminary figures.

Diagram 6.13
GDP deflator
(seasonally adjusted quarter-to-quarter rate of change)



Note : (*) Preliminary figure.

/Notes

Notes :

- (1) On 23 April 2003, the Government announced a package of relief measures to help the community tide over the difficulties caused by the outbreak of SARS in Hong Kong. For households, it includes a rates concession of up to \$1,250 per tenement for the period July to September 2003, as well as a waiver of water and sewage charges of up to \$267 and \$67 respectively per household for the period August to November 2003. These two measures are estimated to have the effect of lowering the Composite CPI by around 0.8 and 0.2 of a percentage point respectively during their implementation periods. For 2003 as a whole, they are estimated to have the combined effect of lowering the Composite CPI by around 0.3 of a percentage point.
- (2) The Consumer Price Indices (A), (B) and (C) are compiled by reference to the average expenditure patterns for different groups of households as enumerated from the Household Expenditure Survey. Then, by aggregating the expenditure patterns of all the households covered by these three indices, a Composite CPI is compiled.

The expenditure ranges of the households covered in the 1999/2000-based CPIs are shown below:

	<u>Approximate proportion of households covered</u> (%)	<u>Monthly expenditure range (at 1999/2000 prices)</u> (\$)
CPI(A)	50	4,500 to 18,499
CPI(B)	30	18,500 to 32,499
CPI(C)	10	32,500 to 65,999

The weightings of the various components in the 1999/2000-based CPIs are as follows:

<u>Expenditure component</u>	<u>Composite CPI</u> (%)	<u>CPI(A)</u> (%)	<u>CPI(B)</u> (%)	<u>CPI(C)</u> (%)
Food	26.67	31.88	25.94	21.38
<i>Meals bought away from home</i>	16.39	17.94	17.20	13.28
<i>Other foodstuffs</i>	10.28	13.94	8.74	8.10
Housing	29.91	29.13	29.68	31.22
<i>Private dwellings</i>	24.59	21.76	25.48	26.67
<i>Public dwellings</i>	2.07	5.08	1.03	--
<i>Maintenance costs and other housing charges</i>	3.25	2.29	3.17	4.55
Electricity, gas and water	2.98	3.99	2.81	2.02
Alcoholic drinks and tobacco	0.94	1.50	0.86	0.39
Clothing and footwear	4.13	3.36	4.47	4.55
Durable goods	6.24	4.96	6.93	6.73
Miscellaneous goods	5.70	5.25	5.58	6.43
Transport	9.01	8.23	9.05	9.94
Miscellaneous services	14.42	11.70	14.68	17.34
All items	100.00	100.00	100.00	100.00

/(3)

- (3) A special one-off rebate was granted by a power company in January and February 2003, at \$250 or at 1.5 cents per unit based on the electricity consumption for the whole year of 2002 per residential customer account, whichever was the higher.

Another special one-off rebate, at half of the electricity consumption in March 2003 with a maximum of \$200 per residential customer account, was granted by the same power company in June and July 2003. This new rebate had the same downward effect on electricity charges for both the second and third quarters of 2003.

- (4) In any particular period, only a small proportion of the tenancies of private dwellings are new lettings for which rentals are freshly determined, and lease renewals upon which rentals are revised. The majority of the tenancies are existing leases with rentals fixed until their expiry. Upon aggregation, the movements in private housing cost, as indicated in the various CPIs, thus tend to be less responsive than the corresponding movements in market rentals, as reflected in the Rating and Valuation Department's rental index for private residential flats.
- (5) The Producer Price Index is designed to reflect changes in the prices of goods and services received by local producers. Producer prices refer to the transacted prices, net of any discounts or rebates allowed to the buyers. Transportation and other incidental charges are not included.
- (6) The terms of trade in goods is defined as the ratio of the prices of total exports of goods to the prices of imports of goods.
- (7) The implicit price deflators of GDP and its main expenditure components are derived by dividing GDP at current prices by the corresponding constant price figures. In compiling the constant price GDP at the finer sub-component level, a standard deflation approach is adopted whereby an appropriate price index is used to deflate each of the sub-components of GDP at current prices. Summing up the individually deflated sub-components gives the main expenditure components of GDP at constant prices. These are further aggregated to arrive at the overall GDP at constant prices. Then, by dividing the current price GDP with the corresponding constant price GDP at the overall level, the GDP deflator is implicitly obtained. Similarly, by dividing each of the main expenditure components of GDP at current prices with each of the corresponding measures at constant prices, the respective price deflators at the main expenditure component level are implicitly obtained. Hence as it stands, the implicit price deflators of GDP and its main expenditure components are not used as input for compiling the corresponding constant price measures. By the same token, the growth rates in real terms of GDP and its main expenditure components are not derived from their corresponding growth rates in money terms using the rates of change in the respective implicit prices deflators. Rather, the growth rates in real terms are calculated directly by comparing the constant price measures over two periods.

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The rate of change in the GDP deflator may differ substantially from that in the Composite CPI over the same time span. The Composite CPI covers consumer price inflation in particular. Yet the GDP deflator is a much broader measure of inflation for the entire economy, and takes into account all the price changes related to consumption, investment, exports and imports. Also, as total final demand in the economy is equated to GDP plus imports, the rate of change in the GDP deflator may differ appreciably from that in the total final demand deflator, depending on the movement in the prices of imports. Likewise, as domestic demand in the economy is equated to GDP plus imports and less exports, the rate of change in the GDP deflator may differ appreciably from that in the domestic demand deflator, depending on the movement in the prices of imports and exports.

STATISTICAL APPENDIX

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Table 1 Gross Domestic Product (GDP) by expenditure component

Expenditure component	(HK\$ million)			
	At current		At constant (2000)	
	<u>market prices</u>		<u>market prices</u>	
	2001 [#]	2002 [#]	2001 [#]	2002 [#]
Private consumption expenditure	765,088 (0.6)	728,429 (-4.8)	775,038 (2.0)	765,846 (-1.2)
Government consumption expenditure	128,863 (7.3)	131,199 (1.8)	127,432 (6.1)	130,479 (2.4)
Gross domestic fixed capital formation	333,115 (-4.1)	292,595 (-12.2)	356,650 (2.7)	341,189 (-4.3)
of which : Building and construction	142,651 (-8.2)	135,361 (-5.1)	153,720 (-1.1)	155,636 (1.2)
Machinery, equipment and computer software	180,090 (-0.1)	147,798 (-17.9)	191,402 (6.2)	173,993 (-9.1)
Change in inventories	-4,060	2,417	-4,889	2,880
Total exports of goods	1,480,987 (-5.8)	1,562,121 (5.5)	1,520,244 (-3.3)	1,651,945 (8.7)
Domestic exports	153,520 (-15.2)	131,079 (-14.6)	162,588 (-10.2)	144,376 (-11.2)
Re-exports	1,327,467 (-4.6)	1,431,041 (7.8)	1,357,656 (-2.4)	1,507,569 (11.0)
less Imports of goods ^(a)	1,549,222 (-5.3)	1,601,527 (3.4)	1,605,267 (-1.9)	1,732,470 (7.9)
Exports of services	307,657 (1.9)	337,949 (9.8)	320,621 (6.2)	359,664 (12.2)
less Imports of services	192,453 (0.5)	193,412 (0.5)	195,447 (2.0)	195,883 (0.2)
Total expenditure on GDP	1,269,975 (-1.4)	1,259,771 (-0.8)	1,294,382 (0.5)	1,323,650 (2.3)
Per capita GDP ^(b) (\$)	188,847 (-2.3)	185,615 (-1.7)	192,476 (-0.4)	195,027 (1.3)
<u>Implicit Price Deflator</u> (2000=100)	<u>Index for</u> <u>2001</u>	<u>% change</u> <u>over 2000</u>	<u>Index for</u> <u>2002</u>	<u>% change</u> <u>over 2001</u>
GDP	98.1	-1.9	95.2	-3.0
Total final demand ^(c)	97.3	-2.7	93.9	-3.5
Domestic demand ^(d)	97.5	-2.5	93.1	-4.5

Notes : Figures in brackets represent percentage changes over a year earlier.

Figures may not add up exactly to the totals due to rounding.

(a) Here imports of goods are valued on f.o.b. basis, instead of on c.i.f. basis as is still the on-going practice for the merchandise trade statistics.

(b) Per capita GDP is equal to total expenditure on GDP divided by the total mid-year population.

(c) Total final demand is defined as the sum of private consumption expenditure, government consumption expenditure, gross domestic fixed capital formation, change in inventories, and exports of goods and services.

(d) Domestic demand is total final demand less exports of goods and services.

(#) Revised figures after incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003.

**Table 2 Gross Domestic Product (GDP) by economic activity
(at current prices)**

Economic activity	At current prices (HK\$ million)		Year-on-year % change		% share in GDP	
	2001	2002 ⁺	2001	2002 ⁺	2001	2002 ⁺
Agriculture and fishing	1,003	1,002	9.0	-0.1	0.1	0.1
Mining and quarrying	174	136	-27.8	-21.8	*	*
Manufacturing	63,519	55,937	-11.4	-11.9	5.2	4.6
Electricity, gas and water	40,126	41,543	3.3	3.5	3.3	3.4
Construction	58,971	53,305	-7.9	-9.6	4.9	4.4
Services	1,051,562	1,057,016	-0.2	0.5	86.5	87.4
Wholesale, retail and import/ export trades, restaurants and hotels	324,654	326,615	*	0.6	26.7	27.0
Transport, storage and communications	124,260	129,371	-1.2	4.1	10.2	10.7
Financing, insurance, real estate and business services	274,030	264,875	-5.9	-3.3	22.5	21.9
Community, social and personal services	265,081	268,218	5.0	1.2	21.8	22.2
Ownership of premises	159,118	158,500	2.5	-0.4	13.1	13.1
<i>less</i> Adjustment for financial intermediation services indirectly measured	95,582	90,562	-0.4	-5.3	7.9	7.5
GDP at factor cost	1,215,354	1,208,940	-1.1	-0.5	100.0	100.0
Taxes on production and imports	53,917	49,787	-6.9	-7.7		
Statistical discrepancy (%)	0.1	0.1	--	--		
GDP at current market prices	1,269,975	1,259,771	-1.4	-0.8		

Notes : Figures may not add up exactly to the totals due to rounding.

(+) Preliminary figures.

(*) Less than 0.05%.

(--) Not applicable.

**Table 3 Gross Domestic Product (GDP) by economic activity
(at constant (2000) prices)**

(HK\$ million)						
Economic activity	2002	2002			2003	
		2nd Qtr	3rd Qtr	4th Qtr	1st Qtr	2nd Qtr [#]
Agriculture and fishing	997 (4.1)	262 (6.9)	226 (2.7)	264 (3.5)	253 (2.8)	268 (2.3)
Mining and quarrying	179 (-13.5)	40 (-20.0)	38 (-30.9)	60 (20.0)	43 (7.5)	45 (12.5)
Manufacturing	59,107 (-9.8)	14,967 (-11.2)	15,953 (-7.3)	14,753 (-9.2)	12,252 (-8.8)	13,096 (-12.5)
Electricity, gas and water	41,030 (3.0)	10,632 (6.9)	12,157 (2.9)	9,736 (0.7)	8,868 (4.3)	10,350 (-2.7)
Construction	60,677 (-1.0)	14,128 (3.2)	15,156 (2.4)	16,516 (-6.4)	14,400 (-3.2)	13,154 (-6.9)
Services	1,104,002 (3.1)	264,713 (1.5)	286,422 (4.3)	295,783 (6.4)	271,370 (5.6)	266,235 (0.6)
Wholesale, retail and import/ export trades, restaurants and hotels	341,835 (5.1)	76,012 (0.5)	94,063 (6.9)	98,035 (14.5)	84,331 (14.4)	80,411 (5.8)
Transport, storage and communications	133,498 (4.0)	31,988 (3.6)	35,141 (5.5)	35,106 (6.2)	32,458 (3.8)	29,912 (-6.5)
Financing, insurance, real estate and business services	292,640 (0.9)	73,282 (0.9)	73,417 (1.6)	75,579 (2.5)	72,250 (2.7)	74,477 (1.6)
Community, social and personal services	264,266 (0.7)	66,359 (0.3)	65,450 (1.1)	68,570 (0.5)	63,648 (-0.4)	63,956 (-3.6)
Ownership of premises	164,468 (2.1)	40,228 (1.4)	41,535 (2.1)	41,816 (1.9)	41,783 (2.2)	41,227 (2.5)
<i>less</i> Adjustment for financial intermediation services indirectly measured	92,705 (-4.1)	23,156 (-4.3)	23,184 (-4.8)	23,325 (-1.6)	23,099 (0.3)	23,748 (2.6)
Taxes on production and imports	57,768 (0.8)	15,403 (1.2)	12,531 (-0.6)	14,833 (2.6)	14,833 (-1.1)	14,748 (-4.3)
Statistical discrepancy (%)	*	-0.7	0.1	0.4	0.5	-0.5
GDP at constant (2000) market prices	1,323,650 (2.3)	317,857 (0.8)	342,983 (3.4)	353,262 (5.1)	323,628 (4.5)	316,363 (-0.5)

Notes : Figures in brackets represent percentage changes over a year earlier.

Figures may not add up exactly to the totals due to rounding.

(#) Revised figures.

(*) Less than 0.05%.

Table 4 Gross National Product (GNP) and external factor income flows (EFIF)

(HK\$ million)

Income component	<u>2002</u>		<u>2002</u>		<u>2003</u>		
			2nd Qtr	3rd Qtr	4th Qtr	1st Qtr	2nd Qtr
(At current market prices)							
Direct investment income							
Inflow total	165,164	(-2.0)	38,871	49,463	37,086	42,497	38,607
Banking	8,539	(4.7)	2,233	2,315	2,309	1,594	1,548
Others ^(a)	156,625	(-2.3)	36,639	47,148	34,777	40,903	37,059
Outflow total	230,854	(-5.7)	55,775	66,561	55,699	53,510	54,185
Banking	61,322	(-2.9)	16,984	13,560	14,197	12,439	13,919
Others ^(a)	169,532	(-6.7)	38,792	53,001	41,502	41,071	40,265
Portfolio investment income							
Inflow total	93,499	(-2.9)	22,622	24,723	20,995	25,673	24,977
Banking	26,394	(-2.5)	6,626	6,704	7,296	7,156	7,207
Others ^(a)	67,105	(-3.1)	15,996	18,019	13,699	18,516	17,769
Outflow total	27,014	(0.7)	10,215	5,563	6,398	3,652	13,046
Banking	4,195	(-8.2)	749	1,363	382	1,648	649
Others ^(a)	22,820	(2.5)	9,466	4,200	6,016	2,004	12,398
Other investment income							
Inflow total	65,421	(-45.4)	16,613	15,638	15,669	13,025	12,145
Banking	56,255	(-45.1)	14,208	13,304	13,602	11,076	10,414
Others ^(a)	9,166	(-47.2)	2,405	2,334	2,067	1,949	1,731
Outflow total	38,793	(-45.9)	9,978	9,600	9,244	8,083	6,958
Banking	32,180	(-49.7)	8,280	8,094	7,058	6,946	6,003
Others ^(a)	6,613	(-15.0)	1,698	1,506	2,186	1,137	956
Compensation of employees							
Inflow total	15	(-50.0)	4	3	2	2	2
Outflow total	15	(-50.0)	4	3	2	2	2
Total EFIF							
Inflow total	324,099	(-15.7)	78,110	89,826	73,751	81,196	75,731
Outflow total	296,676	(-13.6)	75,973	81,726	71,344	65,246	74,191
Net flow total	27,423		2,137	8,099	2,408	15,950	1,539
(At current market prices)							
GNP (\$ million) [#]	1,287,194	(-1.8)	308,360	332,776	332,959	313,792	289,621
Per capita GNP (\$) [#]	189,656	(-2.7)	--	--	--	--	--
(At constant (2000) market prices)							
GNP (\$ million) [#]	1,353,107	(1.2)	320,151	351,791	355,898	341,258	318,084
Per capita GNP (\$) [#]	199,367	(0.3)	--	--	--	--	--

Notes : Figures in brackets represent percentage changes over a year earlier.

Figures may not add up exactly to the totals due to rounding.

(a) Including households, government units, non-profit institutions, and companies other than those in the banking business.

(#) Revised figures.

(--) Not applicable.

Table 5 Balance of payments account

(HK\$ million)

Standard components	2002 [#]	2002		2003		
		2nd Qtr [#]	3rd Qtr [#]	4th Qtr [#]	1st Qtr [#]	2nd Qtr [#]
Current account ⁽¹⁾	118,079	15,046	37,694	39,613	31,495	16,565
Trade in goods	-39,406	-16,381	-4,979	-5,603	-15,985	-9,811
Exports	1,562,121	373,691	435,519	426,824	383,436	419,318
Imports	-1,601,527	-390,072	-440,498	-432,427	-399,421	-429,129
Trade in services	144,537	32,908	38,396	46,382	35,661	28,305
Exports	337,949	78,446	90,499	95,072	82,442	65,504
Imports	-193,412	-45,538	-52,103	-48,690	-46,781	-37,199
External factor income flows	27,423	2,137	8,099	2,408	15,950	1,539
Inflow	324,099	78,110	89,826	73,751	81,196	75,731
Outflow	-296,676	-75,973	-81,726	-71,344	-65,246	-74,191
Current transfers	-14,475	-3,618	-3,822	-3,573	-4,131	-3,469
Inflow	5,357	2,174	1,031	1,076	1,199	1,178
Outflow	-19,831	-5,792	-4,853	-4,649	-5,330	-4,647
Capital and financial account ⁽¹⁾	-191,417	-30,363	-57,056	-57,189	-38,356	-6,276
Capital transfers	-15,725	-7,586	-1,912	-3,229	-1,948	-2,825
Direct investment	-31,007	15,254	-32,735	-3,387	3,016	34,843
Abroad	-137,993	-29,503	-62,429	-5,138	-36,046	17,957
In HK	106,986	44,757	29,694	1,751	39,062	16,886
Portfolio investment	-290,749	-117,765	-82,478	-97,561	-54,803	-25,874
Assets	-283,684	-126,842	-60,200	-83,208	-59,387	-17,178
Liabilities	-7,065	9,076	-22,279	-14,353	4,584	-8,696
Financial derivatives	10,616	6,054	-5,706	-2,048	12,122	22,044
Assets	107,530	23,266	15,343	26,683	62,992	40,460
Liabilities	-96,914	-17,212	-21,049	-28,731	-50,871	-18,416
Other investment	116,906	70,560	58,075	37,454	13,649	-56,198
Assets	324,054	50,015	126,936	50,318	58,386	-6,519
Liabilities	-207,147	20,545	-68,862	-12,863	-44,738	-49,678
Net change in reserve assets ⁽²⁾	18,541	3,120	7,700	11,582	-10,392	21,735
Net errors and omissions	73,338	15,317	19,362	17,576	6,861	-10,289
Overall balance of payments	-18,541 (in deficit)	-3,120 (in deficit)	-7,700 (in deficit)	-11,582 (in deficit)	10,392 (in surplus)	-21,735 (in deficit)

Notes : Figures may not add up exactly to the totals due to rounding.

- (1) In accordance with the balance of payments accounting rules, a positive value for the balance figure in the current account represents a surplus whereas a negative value represents a deficit. In the capital and financial account, a positive value for the balance figure indicates a net inflow and a negative value indicates a net outflow. As increases in external assets are debit entries and decreases are credit entries, a negative value for net change in reserve assets represents a net increase and a positive value represents a net decrease.
- (2) The estimates on net change in reserve assets under the balance of payments framework are transaction figures. Effects from valuation changes (including price changes and exchange rate changes) and reclassifications are excluded.
- (#) Revised figures after incorporating a new set of visitor expenditure figures as released by the Hong Kong Tourism Board near end-November 2003.

**Table 6 Major economic indicators in the external sector
for the third quarter of 2003**

Statistical variable	Unit of denomination	Magnitude	% change over	
			Previous period	Same period last year
<u>Value</u>				
Re-exports	\$Mn	430,582	10.3	8.2
Domestic exports	\$Mn	35,081	22.9	-5.4
Total exports of goods	\$Mn	465,662	11.2	7.1
Imports of goods	\$Mn	473,123	9.5	6.1
Visible trade balance	\$Mn	-7,461	--	--
<u>Unit value indices</u> (2000 = 100)				
Re-exports		93.6	-0.5	-2.0
to :	Mainland of China	93.3	-0.8	-1.8
	United States	96.0	0.3	-0.9
	Japan	93.8	-0.4	-2.0
	United Kingdom	93.7	0.2	-2.2
	Germany	92.6	-0.4	-3.1
Domestic exports		92.8	0.6	0.3
to :	United States	100.4	1.0	4.2
	Mainland of China	88.4	*	-0.9
	United Kingdom	94.9	-0.1	-1.1
	Taiwan	83.8	1.5	1.2
	Germany	91.1	3.4	-0.5
Imports of goods		92.4	-0.2	-0.9
from :	Mainland of China	95.0	0.1	-0.1
	Japan	94.1	-0.2	0.9
	Taiwan	89.7	-0.7	-1.3
	United States	92.0	0.4	-1.1
	Republic of Korea	84.0	-2.1	-6.0
of :	Raw materials and semi-manufactures	91.5	0.2	0.9
	Consumer goods	96.7	0.6	0.6
	Capital goods	87.7	-2.1	-5.6
	Foodstuffs	92.3	1.0	0.1
	Fuels	99.4	0.7	7.0

Notes : Figures may not add up exactly to the totals due to rounding.

(--) Not applicable.

(*) Change of less than 0.05%.

**Table 6 Major economic indicators in the external sector
for the third quarter of 2003 (cont'd)**

Statistical variable	Magnitude	% change over	
		Previous period	Same period last year
<u>Terms of trade index</u> (2000 = 100)	101.1	-0.2	-0.9
<u>Quantum indices</u> (2000 = 100)			
Re-exports	134.1	11.2	11.3
<i>to :</i> Mainland of China	164.9	8.4	21.3
United States	108.5	18.4	-6.1
Japan	123.0	12.4	13.7
United Kingdom	117.8	25.6	8.0
Germany	114.7	15.4	13.8
Domestic exports	84.6	22.0	-5.4
<i>to :</i> United States	93.3	47.8	-7.1
Mainland of China	86.2	12.2	-2.9
United Kingdom	91.4	28.5	0.7
Taiwan	66.6	16.0	-21.3
Germany	61.1	9.2	15.6
<i>of :</i> Textiles and clothing	106.4	36.6	-3.5
Products other than textiles and clothing	64.6	5.1	-8.2
Imports of goods	125.5	10.0	7.9
<i>from :</i> Mainland of China	127.2	13.1	6.5
Japan	117.6	7.9	11.0
Taiwan	118.1	9.0	4.8
United States	95.8	2.8	2.8
Republic of Korea	142.2	15.7	22.8
<i>of :</i> Raw materials and semi-manufactures	126.2	2.9	7.3
Consumer goods	118.9	18.0	2.3
Capital goods	138.9	10.6	17.8
Foodstuffs	98.4	11.2	-0.9
Fuels	108.4	18.4	1.9

Table 7 Major economic indicators in the domestic economy

Statistical variable	Unit of Denomination	Magnitude	% change over	
			Previous period	Same period last year
<u>Manufacturing sector</u> (2nd Qtr 2003)				
Index of Industrial Production (2000 = 100)		78.1	10.8	-12.5
<u>Property</u> (3rd Qtr 2003)				
Completions of new property				
for : Residential	no. of units	9 816	50.8	-26.5
Commercial	'000 sq. m	41	-78.1	-17.4
of which :				
Office space	'000 sq. m	28	-82.4	224.4
Other commercial Premises	'000 sq. m	13	-52.9	-68.6
Industrial	'000 sq. m	0	--	--
of which :				
Industrial-cum-office Premises	'000 sq. m	0	--	--
Flatted factory space	'000 sq. m	0	--	--
Storage premises	'000 sq. m	0	--	--
Floor area of building consents				
for : Residential	'000 sq. m	186	-6.5	1.0
Commercial	'000 sq. m	71	200.0	-47.8
Industrial	'000 sq. m	#	--	-84.6
Others	'000 sq. m	191	59.0	300.0
Total	'000 sq. m	448	30.7	21.7
<u>Building and construction</u> (2nd Qtr 2003)				
Labour and Material Cost Index (mid-Feb 1970 = 100)		1 739	-0.9	-1.0
Tender Price Indices (Jan 1970 = 100)				
for : Public sector building projects		723	0.4	-2.6
Public housing projects		474	-0.4	-11.1
<u>Electricity consumption</u> (3rd Qtr 2003)				
for : Industrial	Mn KWh	1 113	0.3	-10.7
Commercial	Mn KWh	7 253	16.8	3.3
Domestic	Mn KWh	3 644	60.5	2.7
<u>Gas consumption</u> (3rd Qtr 2003)				
for : Industrial	Terajoule	265	9.5	8.2
Commercial	Terajoule	2 512	0.2	-4.0
Domestic	Terajoule	3 163	-26.6	6.0

Notes : Figures may not add up exactly to the totals due to rounding.

(#) Less than 500 sq. m.

(--) Not applicable.

Table 7 Major economic indicators in the domestic economy (cont'd)

Statistical variable	Unit of denomination	Magnitude	% change over	
			Previous period	Same period last year
<u>Transport</u>				
Passenger journeys (3rd Qtr 2003)				
by : KMB	'000	268 495	11.2	-4.6
NWFB	'000	45 999	10.5	-6.5
City Bus	'000	53 177	14.6	-4.4
New Lantau Bus	'000	2 559	23.0	8.9
Long Win Bus	'000	5 126	26.8	-4.7
MTR	'000	203 230	21.2	1.1
KCR	'000	72 068	20.3	-3.0
LRT	'000	27 104	14.2	-3.4
Hong Kong Tramways	'000	20 260	9.3	-4.3
New World First Ferry	'000	3 580	5.5	-3.5
Star Ferry	'000	6 971	26.8	-0.9
Private cars licensed				
new registration (3rd Qtr 2003)	no.	5 813	22.8	-31.2
total licensed (end-Sep 2003)	no.	338 201	-0.1	-0.7
Air passenger movements (3rd Qtr 2003)	'000	5 690	194.8	-6.1
Air cargo (3rd Qtr 2003)	'000 tonne	665	9.9	4.9
Ocean cargo (2nd Qtr 2003)	'000 tonne	36 701	3.1	3.8
Container throughput (2nd Qtr 2003)	'000 TEUs	5 090	8.5	7.1
<u>Tourism</u>				
Arrivals of incoming visitors (3rd Qtr 2003)	'000	4 415	168.2	4.1
Departures of Hong Kong residents (3rd Qtr 2003)	'000	16 769	35.8	0.3
to : Mainland of China	'000	14 212	33.0	-0.4
Macau	'000	1 169	36.6	2.7
Other countries	'000	1 387	73.0	5.9
Hotel rooms (end-Sep 2003)	no.	42 848	0.1	0.2
Hotel room occupancy rate (3rd Qtr 2003)	%	80	220.0	-3.6
<u>Telecommunications (end-Sep 2003)</u>				
Telephone lines	Mn	3.8	*	-1.2
for : Residential users	Mn	2.1	-0.4	-0.9
Business users	Mn	1.7	0.5	-1.7
Facsimile lines	'000	500	-2.9	-11.4
Public mobile radiotelephone services customers	'000	6 754	4.2	14.3

Notes : Figures may not add up exactly to the totals due to rounding.

(*) Change of less than 0.05%.

**Table 8 Major economic indicators in the financial sector
as at end-September 2003**

Statistical variable	Unit of denomination	Magnitude	% change over	
			Previous period	Same period last year
<u>Exchange rate</u>				
Effective Exchange Rate Indices of the Hong Kong dollar (Jan 2000 = 100)				
trade-weighted		99.9	-0.9	-3.2
import-weighted		100.6	-1.4	-3.2
export-weighted		99.1	-0.5	-3.3
HK\$/US\$ interbank T/T rate	HK\$	7.743	-0.7	-0.7
<u>Interest rate</u>				
3-month HIBOR	%	0.69	--	--
Savings rate	%	0.03	--	--
Best lending rate	%	5.00	--	--
<u>Monetary statistics</u>				
Money supply : M1	\$Mn	349,192	8.7	27.5
M2	\$Mn	3,671,198	2.4	5.8
M3	\$Mn	3,712,282	2.4	5.6
Deposits with :				
licensed banks	\$Mn	3,393,526	2.5	4.6
restricted licence banks	\$Mn	34,489	-2.8	-10.6
deposit-taking companies	\$Mn	5,231	-5.4	-8.4
all authorized institutions	\$Mn	3,433,245	2.5	4.4
Deposits by type :				
demand	\$Mn	226,228	12.4	37.6
savings	\$Mn	1,098,080	6.4	23.1
time	\$Mn	2,108,938	-0.4	-5.5
total	\$Mn	3,433,245	2.5	4.4

Notes : Figures may not add up exactly to the totals due to rounding.

(--) Not applicable.

**Table 8 Major economic indicators in the financial sector
as at end-September 2003 (cont'd)**

Statistical variable	Unit of denomination	Magnitude	% change over	
			Previous period	Same period last year
Loans and advances by :				
licensed banks	\$Mn	1,891,476	-1.7	-3.2
restricted licence banks	\$Mn	101,065	-2.0	-12.9
deposit-taking companies	\$Mn	25,414	-1.3	-9.9
all authorized institutions	\$Mn	2,017,955	-1.7	-3.8
Loans and advances by all authorized institutions :				
to finance imports to, exports and re-exports from Hong Kong	\$Mn	87,408	-0.9	2.9
to finance merchandising trade not touching Hong Kong	\$Mn	9,807	-5.4	4.9
other loans for use in Hong Kong	\$Mn	1,690,551	-1.8	-3.2
other loans for use outside Hong Kong	\$Mn	212,380	-2.3	-14.2
other loans where the place of use is not known	\$Mn	17,809	8.9	96.4
<u>Stock market</u>				
Hang Seng Index (31 Jul 1964 = 100)		11 230	17.3	23.8
Stock market capitalisation				
Main Board	\$Mn	4,708,475	20.5	41.5
Growth Enterprise Market	\$Mn	67,987	11.5	27.3
Total	\$Mn	4,776,462	20.4	41.3
Stock market turnover (3rd Qtr 2003)				
Main Board	\$Mn	752,607	57.9	101.3
Growth Enterprise Market	\$Mn	14,177	85.6	41.3
Total	\$Mn	766,784	58.3	99.7

Note : Figures may not add up exactly to the totals due to rounding.

Table 9 Major economic indicators in the labour sector

Statistical variable	Unit of denomination	Magnitude	% change over	
			Previous period	Same period last year
<u>Labour force characteristics</u> (3rd Qtr 2003)				
Labour force	'000	3 492	-0.8	-0.7
Unemployed	'000	297	-0.9	10.9
Underemployed	'000	127	-16.2	24.8
Employed	'000	3 195	-0.8	-1.7
Labour force participation rate	%	61.2	--	--
Seasonally adjusted unemployment rate	%	8.3	--	--
Underemployment rate	%	3.6	--	--
<u>Employment</u> (Jun 2003)				
Manufacturing	'000	172	-3.6	-13.8
Services	'000	1 949	-0.8	-2.2
<i>of which :</i>				
Wholesale, retail and import/export trades	'000	767	-0.8	-0.9
Restaurants and hotels	'000	191	-3.6	-10.6
Transport, storage and Communications	'000	171	-0.9	-6.7
Financing, insurance, real estate and business services	'000	419	-0.8	-2.6
Community, social and personal services	'000	401	0.6	2.5
Building and construction sites	'000	63	-5.3	-20.2
Civil service	'000	168	-0.5	-2.0
<u>Vacancies</u> (Jun 2003)				
Manufacturing	'000	1	14.1	-16.4
Services	'000	20	31.9	-3.9
<i>of which :</i>				
Wholesale, retail and import/export trades	'000	6	18.0	-13.8
Restaurants and hotels	'000	1	33.0	-22.3
Transport, storage and Communications	'000	1	13.0	-8.1
Financing, insurance, real estate and business services	'000	6	48.7	3.2
Community, social and personal services	'000	5	38.7	11.0
Building and construction sites	'000	#	3.8	-52.6
Civil Service	'000	2	3.7	-13.5

Notes : Figures may not add up exactly to the totals due to rounding.

(--) Not applicable.

(#) Less than 500.

Table 9 Major economic indicators in the labour sector (cont'd)

Statistical variable	Magnitude	% change over	
		Previous period	Same period last year
<u>Earnings</u> (2nd Qtr 2003)			
Nominal index of payroll per person engaged (Q1 1999 = 100)	86.5	-13.7 (-12.9)	-2.5 (-0.1)
<i>for</i> : Manufacturing	86.5	-11.3 (-10.5)	-2.2 (0.3)
Services	85.2	-14.2 (-13.4)	-3.0 (-0.6)
<i>of which</i> :			
Wholesale, retail and Import/export trades	80.8	-20.4 (-19.6)	-2.5 (*)
Restaurants and hotels	72.6	-14.6 (-13.8)	-9.8 (-7.6)
Transport, storage and Communications	85.5	-13.8 (-13.0)	-3.8 (-1.4)
Financing, insurance, real Estate and business services	84.6	-13.4 (-12.7)	-1.5 (0.9)
Community, social and Personal services	90.5	-5.5 (-4.6)	-4.6 (-2.2)
<u>Wages</u> (Jun 2003)			
Nominal wage index (Sep 1992 = 100)	147.1	-0.7 (1.0)	-2.5 (-0.1)
<i>for</i> : Manufacturing	144.1	0.6 (2.3)	-2.4 (*)
Services			
<i>of which</i> :			
Wholesale, retail and Import/export trades	156.8	-0.8 (0.8)	-2.9 (-0.5)
Restaurants and hotels	128.8	-2.1 (-0.5)	-4.5 (-2.1)
Transport services	147.9	-0.8 (0.9)	-2.0 (0.4)
Financing, insurance, real Estate and business services	155.3	0.4 (2.1)	-0.9 (1.5)
Personal services	147.1	-2.0 (-0.3)	-2.8 (-0.3)
Nominal index of construction wage rate (Jan 1970 = 100) (Aug 2003)	3 544.4	-0.7 (-0.6)	-0.7 (2.9)

Notes : Figures in brackets represent percentage changes in real terms.

(*) Change of less than 0.05%.

Table 10 Various price indices for the third quarter of 2003

Statistical variable	Magnitude	% change over	
		Previous period	Same period last year
<u>Consumer Price Indices</u> (Oct 1999 - Sep 2000 = 100)			
Composite CPI	91.1	-1.9 [#]	-3.6
CPI(A)	91.3	-2.3 [#]	-3.3
CPI(B)	90.9	-1.8 [#]	-3.7
CPI(C)	91.0	-1.6 [#]	-4.1
<u>Property Price Indices</u> (1999 = 100)			
Residential flats	58.4	-1.8	-14.9
Office space	58.9	0.3	-14.1
Shopping space	82.7	0.9	-3.9
Conventional flatted factory space	68.3	-2.3	-8.2
<u>GDP deflator</u> ⁺ (2000 = 100)	89.3	-1.2 [#]	-5.7

Notes : (+) Preliminary figures.

(#) Seasonally adjusted series.