

# High Frequency Macroeconomic Forecasts

## Current Quarter Model: 2001Q2

APEC Study Center  
The University of Hong Kong

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The Hong Kong economy will revert to a more normal growth path after its full recovery in 2000. Real GDP is forecasted to grow at 3.3% and 3.8% in the first quarter and the second quarter of 2001 respectively, according to the High Frequency Macroeconomic Forecast carried by the APEC Study Centre of The University of Hong Kong.

The main concern is the impact of the slow-down of the U.S. economy on Hong Kong external trade performance. Meanwhile, the cutting of U.S. interest rates by the Fed is expected to have positive effects on the consumption and investment situations in Hong Kong.

The contributions of individual component to the real GDP growth are shown by the following decomposition:

Component	00Q2	00Q3	00Q4	01Q1	01Q2
Private Consumption	3.1	3.1	1.5	1.1	0.8
Government Consumption	0.2	0.2	0.0	0.2	0.2
Merchandise Trade	-3.1	-1.8	-0.6	0.8	-3.6
Service Trade	4.4	3.4	2.5	1.4	0.7
Investment in Land and Construction	-1.8	-0.3	-0.2	-0.1	0.0
Investment in Machinery and Equipment	3.2	4.1	3.4	1.5	1.9
Inventory Investment	4.9	2.1	0.2	-1.5	3.8
GDP	10.8	10.8	6.8	3.3	3.8

A major contribution to output growth came from the investment in machinery and equipment which accounted for 3.4 percentage points of the growth of 6.8% in the fourth quarter. It continued to contribute a major part to output growth accounting for 1.5 percentage points of the 3.3% forecasted growth in the first quarter and for 1.9 percentage points of the 3.8% in the second quarter. As the investment in machinery and equipment helps to raise labour productivity, this would prepare Hong Kong for better growth in the future.

Another major contribution to output growth came from the trade in services. It accounted for 2.5 percentage points of the 6.8% growth in the fourth quarter of 2000. It is expected to account for 1.4 percentage points of the 3.3% forecasted growth in the first quarter and for 0.7 percentage in the second quarter of 2001. As Mainland of China will enter the WTO in the near future, the importance of trade in services to output growth is expected to increase.

Inventory investment is expected to be very important as a source of growth in the second quarter of 2001. It is expected to account for nearly all of the growth in real output in the second quarter.

The forecast details are in Table 1 and Table 2, and the forecasts of selected monthly indicators are in Table 3.

## **Forecast Highlights**

The highlights of our current forecasts are:

- Private consumption spending grew by 2.8% in the fourth quarter of 2000. As the economy slows down, the consumption spending will continue to be slack. The rate is forecasted to be 1.8% in the first quarter, and is expected to be 1.4% in the second quarter of 2001.
- Consumption growth has been slower than income growth throughout last year, implying that gross saving rate was increasing. The gross saving rate was 37.6% in 2000. This is the highest point since 1988. Households continue to save to rebuild their financial portfolios. As the interest rates continue to decrease, the saving rate should go down and the private consumption spending is expected to pick up in the second half of 2001.
- The growth in retail sales remained sluggish. Notwithstanding the Lunar New Year celebration, the volume of retail sales only grew by 2.5% in January 2001 compared to a year ago. Clothing, footwear and clothing accessories were still the major category with strong growth in the volume. The year-on-year rate was 12.4% in January. This may due to the effect of price discount as the retail price of the category dropped by 7.5% in the same period.
- The growth in external trade is expected to slow in 2001. The effect of slow-down in the U.S. economy on external trade was first revealed in last November. The growth rate of re-exports dropped from 25.8% in October to 11.8% in November. Meanwhile, the growth rate of domestic exports moved from positive 15.8% to negative 5.4%. As global demand continued to be weak with the slow-down of the U.S. economy. Re-export is predicted to grow by 9.1% in the first quarter and by 9.3% in the second quarter of 2001 respectively. Domestic export of goods is expected to be level off and grows by 0.1% in both the first and second quarter of 2001.

- After a long period of double-digit growth in last year, the number of visitor arrivals is expected to be moderate this year. The growth rate was 4.1% in February. As external trade is slackened this year, export of services is expected to grow by 6.6% in the first quarter and by 3.6% in the second quarter of 2001 respectively.
- In tandem with the growth in re-export and domestic spending, the import of goods is estimated to grow by 7.1% and 9.7% in the first and the second quarter of 2001 respectively.
- The growth of investment spending in machinery and equipment was very strong with rate at 24.6% for the whole of 2000. The sustainable growth should continue though at a slower rate. The rate is predicted at 9.9% in the first quarter. It is expected to grow by 10.8% in the second quarter of 2001.
- The recovery of the property market has been uneven last year. However as the mortgage rates continue to decrease, residential housing is becoming increasingly affordable. Investment on land and construction has shrunk by 8.3% in 2000. The rate of decline has moderated since the third quarter of last year. The drop is estimated to be 1.1% and 0.1% in the first quarter and the second quarter of 2001 respectively.
- We are still in the process of climbing out of deflation. Prices are basically stable except for the clothing and footwear, and housing sectors. In February, these two components of the Composite CPI drop by 7.7% and 3.5% respectively. But the drop in the housing component does not mean residential rents are falling. Compared with the levels in 1999, rents had been quite stable throughout last year. The private domestic rental index dropped by only 1.9% in 2000 compared to 1999. The drop in the CPI housing component is due to lower rents of new leases, and thus reflects the large drop in rents in 1998. Excluding housing, the deflation rate would only be 1.5%, instead of the 2.1% in February. The deflation rate is forecasted to be 1.8% and 1.9% in the first quarter and the second quarter of 2001 respectively.
- With the slackening in the economy, the improvement in employment situation will be slower. The unemployment rate will be at similar level as the fourth quarter of 2000. It is projected to be at 4.5% and 4.6% in the first quarter and the second quarter of 2001 respectively. Unemployment is still concentrated in the construction sector, with rate at 9.9% in the fourth quarter of 2000.
- However, the continued shortening of unemployment duration can be regarded as a positive sign on the employment front. For example, the number of workers unemployed for more than 6 months went from 68,100 in the fourth quarter of 1999 down to 35,400 in the fourth quarter of 2000. In the same period, the number unemployed between 3 and 6 months dropped from 40,600 to 27,900. There is no evidence to support the worsening of long-term unemployment.

## **Concluding Remarks**

The slowdown of the U.S. economy, coupled with still sluggish economic performance in Japan, will drag down the growth of the Hong Kong economy in the next couple of quarters. Lower interest rates will help to stimulate domestic spending in consumption and investment, as well as easing the financing burdens of debtors, but it will take 6 to 12 months before the positive effects beginning to have an impact on the real economy. Hong Kong has to prepare for a slower growth environment.

## **About Our Model**

Our forecasting system was developed in collaboration with Professor Lawrence Klein of the Wharton School of the University of Pennsylvania, and is partially funded by the Better Hong Kong Foundation. Researchers at the APEC Study Center of The University of Hong Kong are solely responsible for accuracy and interpretation of the forecasts. Our quarterly forecasts can be accessed at <http://www.hku.hk/apec/cqm/>.

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Table 1: Current Quarter Model Forecast  
(Million of 1990 Dollar)

	2000				2001	
	Q2	Q3	Q4	Annual	Q1 (forecast)	Q2 (forecast)
Gross Domestic Product	213362	235326	235870	893650	216060	221430
Private Consumption Expenditure	121592	124724	125366	492461	122991	123313
Government Consumption Expenditure	15660	16180	16239	65534	17891	16052
Domestic Exports of Goods	46184	50498	46055	185928	43232	46207
Re-exports of Goods	350328	394432	391299	1445216	337192	382868
Imports of Goods	414015	454008	445779	1683831	396484	454236
Exports of Services	62247	70161	71809	263428	63109	64477
Imports of Services	34809	38595	36242	144852	36235	35613
Investment in Land & Construction	23739	26285	25991	102608	26303	23721
Investment in Machinery & Equipment	37637	40950	39768	150398	35208	41707
Changes in Inventories	4799	4699	1364	16760	2854	12936
Date of Forecast: Apr 2, 2001						

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Table 2: Current Quarter Model Forecast						
Year-on-Year Growth Rate (%)						
	2000				2001	
	Q2	Q3	Q4	Annual	Q1 (forecast)	Q2 (forecast)
Gross Domestic Product	10.8	10.8	6.8	10.5	3.3	3.8
Private Consumption Expenditure	5.0	5.6	2.8	5.4	1.8	1.4
Government Consumption Expenditure	2.7	2.5	-0.6	2.1	2.5	2.5
Domestic Exports of Goods	8.3	8.2	-0.8	7.5	0.1	0.1
Re-exports of Goods	19.1	19.0	15.2	18.5	9.1	9.3
Imports of Goods	18.8	18.4	13.4	18.1	7.1	9.7
Exports of Services	18.3	14.1	10.4	14.3	6.6	3.6
Imports of Services	3.7	3.8	3.3	2.6	2.9	2.3
Investment in Land & Construction	-12.7	-2.3	-1.4	-8.3	-1.1	-0.1
Investment in Machinery & Equipment	19.5	26.9	23.3	24.6	9.9	10.8
GDP Deflator Growth Rate	-7.5	-6.4	-5.3	-6.6	-3.8	-2.3
CPI (Composite) Inflation Rate	-4.5	-2.8	-2.2	-3.7	-1.8	-1.9
Unemployment Rate	5.0	4.8	4.4	5.0	4.5	4.6
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Table 3: Selected Monthly Indicators  
Year-on-Year Growth Rate (%)

	2000						2001					
	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN
Unit Value Trade Index (Domestic Exports)	-0.5	0.2	-0.1	-0.8	-0.7	-1.9	-1.7	-1.9	-1.4	-1.2	-0.8	-1.3
Unit Value Trade Index (Imports of Foodstuffs)	-4.4	-2.9	-2.6	-1.9	-1.7	-2.2	-0.8	-0.8	-0.2	0.6	0.3	1.4
Unit Value Trade Index (Imports of Consumer Goods)	-1.9	-1.6	-1.4	-0.8	-1.3	-1.8	-0.1	-0.9	0.5	1.1	2.0	1.5
Unit Value Trade Index (Imports of Raw Materials & Semi-Manufactures)	2.6	2.4	2.8	1.9	0.9	-0.1	0.1	0.1	-0.2	-1.1	-1.1	-0.8
Unit Value Trade Index (Imports of Capital Goods)	0.6	-0.7	-2.4	-3.6	-3.4	-4.0	-2.8	-1.9	-2.3	-2.2	-1.3	-1.5
Real Retained Imports of Foodstuffs	-10.1	4.1	8.1	2.2	-6.9	-3.8	-5.7	-7.1	6.1	14.5	-8.2	-10.6
Real Retained Imports of Consumer Goods	20.5	46.0	30.7	-38.8	22.3	4.3	-47.8	-2.3	-22.5	-16.3	-22.4	-22.1
Real Retained Imports of Raw Materials & Semi-Manufactures	16.9	22.2	19.7	25.2	14.5	-6.3	-1.8	-4.1	-1.6	4.9	7.7	10.5
Real Retained Imports of Fuels	-48.9	-7.2	-20.6	-15.5	8.4	-10.8	-4.0	-3.6	28.8	9.1	-0.6	25.7
Real Retained Imports of Capital Goods	15.2	65.5	28.5	72.4	14.9	43.5	20.6	28.4	2.3	25.2	5.0	25.0
Total Motor Vehicles Newly Registered	23.1	19.4	-0.7	14.6	19.0	25.4	-10.0	21.2	-5.1	16.8	1.1	4.4
Private Cars Newly Registered	23.9	11.0	-12.4	0.9	8.2	11.7	-20.0	17.8	-19.7	2.0	-11.9	-3.7
Volume Index of Retail Sales	4.1	5.5	8.0	3.5	1.2	2.6	2.5	3.2	-1.3	-3.9	-1.5	0.4
Electricity Consumption	5.5	2.9	10.0	9.0	6.8	1.4	6.4	1.7	2.6	10.7	1.6	-0.3
Gas Consumption	3.6	5.3	5.5	6.0	6.2	6.8	3.2	2.9	2.9	2.5	3.1	2.0
Hong Kong Resident Departures	11.9	15.1	18.0	6.0	12.3	9.5	20.3	2.8	10.7	3.5	8.0	6.5
Visitors Arrivals	13.4	15.8	22.5	13.0	7.2	18.5	7.9	4.1	7.3	2.9	4.7	5.5
Money Supply (Definition 2)	8.3	10.8	8.7	8.6	9.1	8.8	8.6	7.8	8.6	9.4	10.8	9.5
Loans and Advances	-11.7	-8.5	-11.5	-10.8	-11.6	-12.5	-11.2	-10.8	-11.3	-10.0	-9.2	-9.5
Land Considerations	-17.7	18.7	13.1	-17.2	-5.7	21.0	-30.5	-8.0	-4.0	-9.5	10.9	9.4
Effective Exchange Rate Index	-0.9	0.7	1.9	3.2	3.4	3.6	3.8	3.0	3.1	3.2	2.1	2.9
Hang Seng Index of Shares Prices	26.2	31.1	21.9	18.4	4.4	-7.5	-1.3	-6.3	-22.9	-18.6	-12.0	-19.5

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