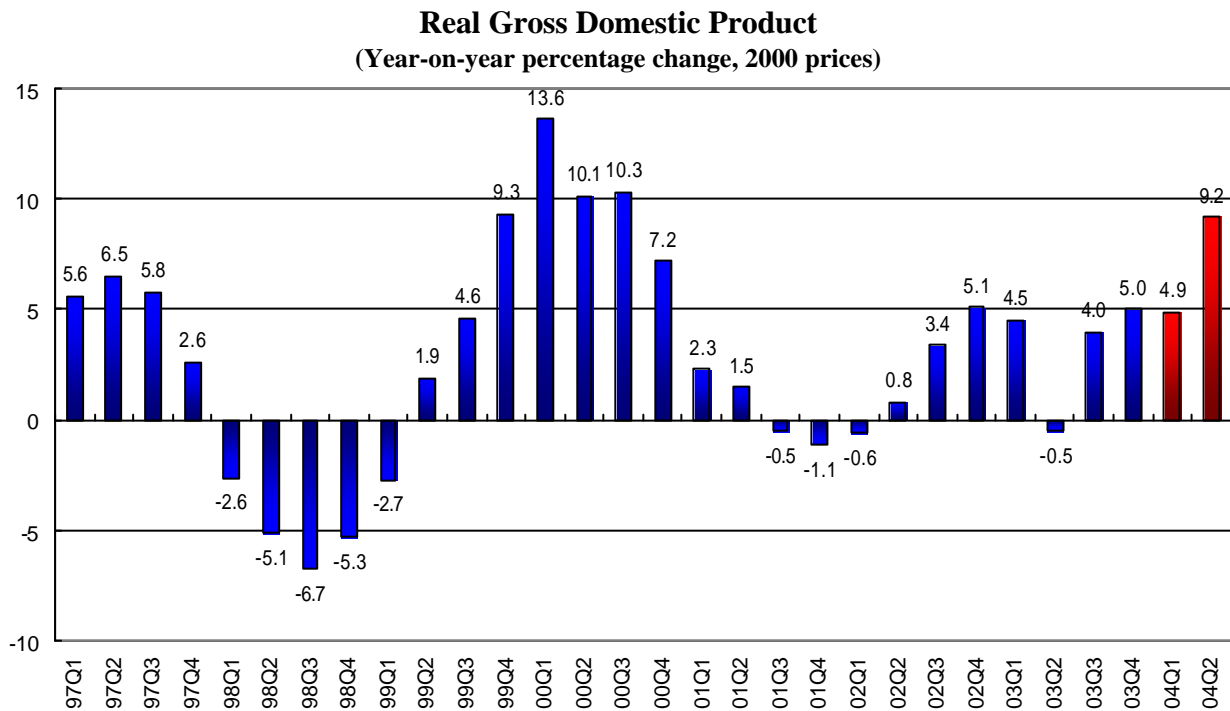


# High Frequency Macroeconomic Forecasts Current Quarter Model: 2004Q2

APEC Study Center  
The University of Hong Kong

April 7, 2004

## Economic Recovery Continues



Hong Kong's economic recovery was disrupted by SARS in the second quarter of last year, with the economy contracted by -0.5% year-on-year. Since then, the economy has bounced back with real GDP growing by 4.0% and 5.0% in the last two quarters of last year. Given the improving global economy and strong growth in Asia, external demand for Hong Kong's goods and services is expected to continue to have robust growth. The weak US dollar has helped to strengthen Hong Kong's external competitiveness. More importantly, domestic demand, particularly private consumption spending boosted by the positive economic outlook and the recovery in the property market, will also continue to improve. The current economic recovery will thus be more broadly based, depending on both external and domestic demand.

According to the High Frequency Macroeconomic Forecast carried by the APEC Study Center of The University of Hong Kong, real GDP is estimated to increase by 4.9% in the first quarter of 2004, on a year-on-year basis, and is projected to grow by 9.2% in the second quarter of 2004 from the low base of last year. For the first half of 2004, real GDP is forecast to grow by 7.0% as compared with the first half of last year.

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

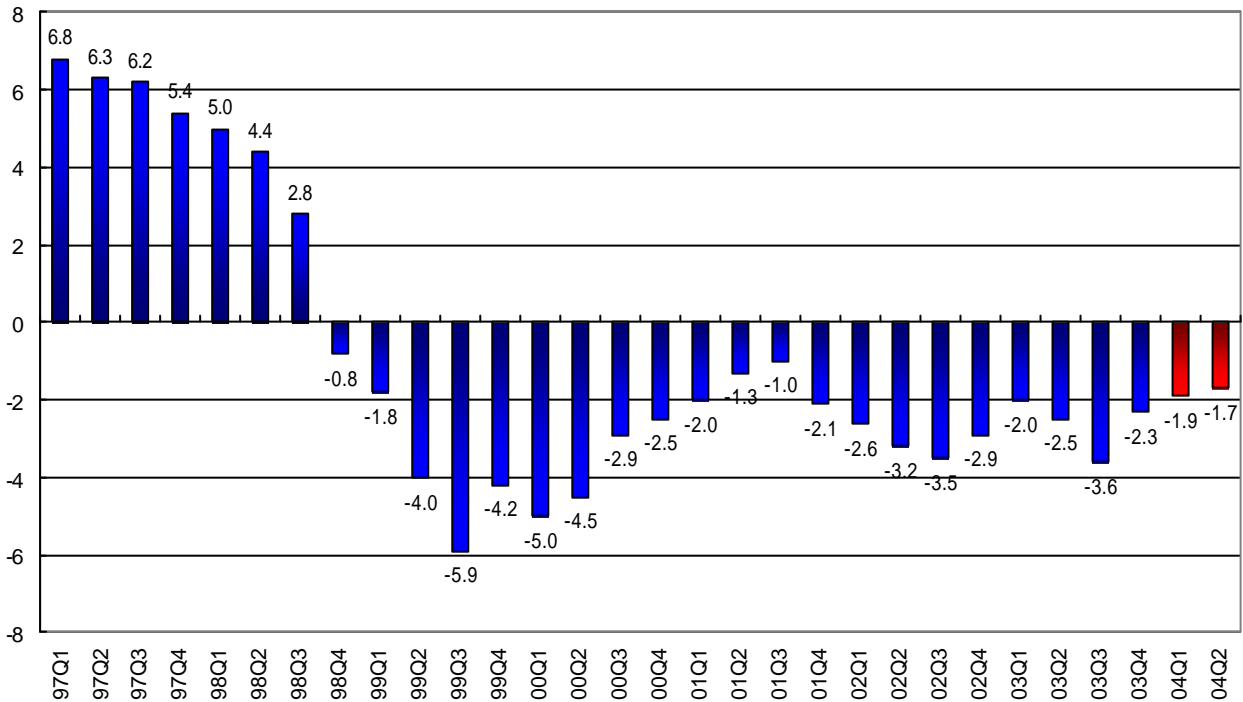
## Forecast Highlights

The highlights of our current forecasts are:

- Private consumption spending increased by 3.6% in the fourth quarter of 2003. Buoyed by improving consumer sentiment underpinned by the rebound of the property market, it is projected to continue to expand by 5.1% in the first quarter of 2004 and by 6.1% in the second quarter of 2004, on a year-on-year basis.
- The volume of retail sales grew by 2.9% year-on-year in January 2004 for the sixth consecutive month. Due to the continued strengthening of local demand and the surge in visitor arrivals from the Mainland, the volume of retail sales is forecasted to pick up noticeably in the first and second quarters of 2004 by growing at 5.7% and 11.6% respectively, both on a year-on-year basis.
- Domestic exports shrank by 0.2% in the fourth quarter of 2003. It is forecasted to contract in the coming quarters, dropping by 3.4% in the first quarter and 1.0% in the second quarter of 2004, on a year-on-year basis.
- Re-exports recorded strong growth of 16.0% in the fourth quarter of 2003 on a year-on-year basis. Given the improving global economy and strong economic growth in Asia, growth in re-exports is projected to continue in the first quarter of 2004 at an annual rate of 14.5%, and is forecasted to moderate to 12.5% in the second quarter of 2004.
- Given the higher global demand and the rapid growth in the number of visitors from the Mainland, exports of services registered a double-digit growth of 11.8% in the fourth quarter of 2003. Comparing with the same period last year, the total number of visitor arrivals surged by 32.6% in January, with hotel occupancy rate kept at 78%. The export of services is estimated to grow by 9.9% in the first quarter of 2004. The growth is forecasted to rise sharply to 36.0% in the second quarter of 2004 due to the lower base of comparison.
- Imports of goods grew by 15.7% in the fourth quarter of 2003 on an annual basis. Retained import of goods is expected to increase to support the economic recovery. The growth in the imports of goods is projected to be 14.8% in the first quarter and 13.4% in the second quarter of 2004.
- Imports of services went up by 4.2% in the fourth quarter of 2003. The number of resident departures grew by 2.0% in December 2003 but dropped by 1.4% in January 2004 due to the Chinese Lunar New Year fell in January this year but in February last year. The growth is expected to pick up sharply in the upcoming months. Service import is projected to go up by 5.6% in the first quarter of 2004. The growth will pick up further to 27.6% in the second quarter 2004 due to the lower base of comparison.
- The trade balance, as measured by the net exports of goods and services, was estimated to be 11.1% of GDP in the fourth quarter of 2003. Imports of goods retained for local use had been increasing in the first 2 months of 2004, thus enlarging the deficits in the net exports of goods. The net trade balance is forecasted to shrink to 4.1% of GDP in the first quarter of 2004 and to 6.8% of GDP in the second quarter of 2004.

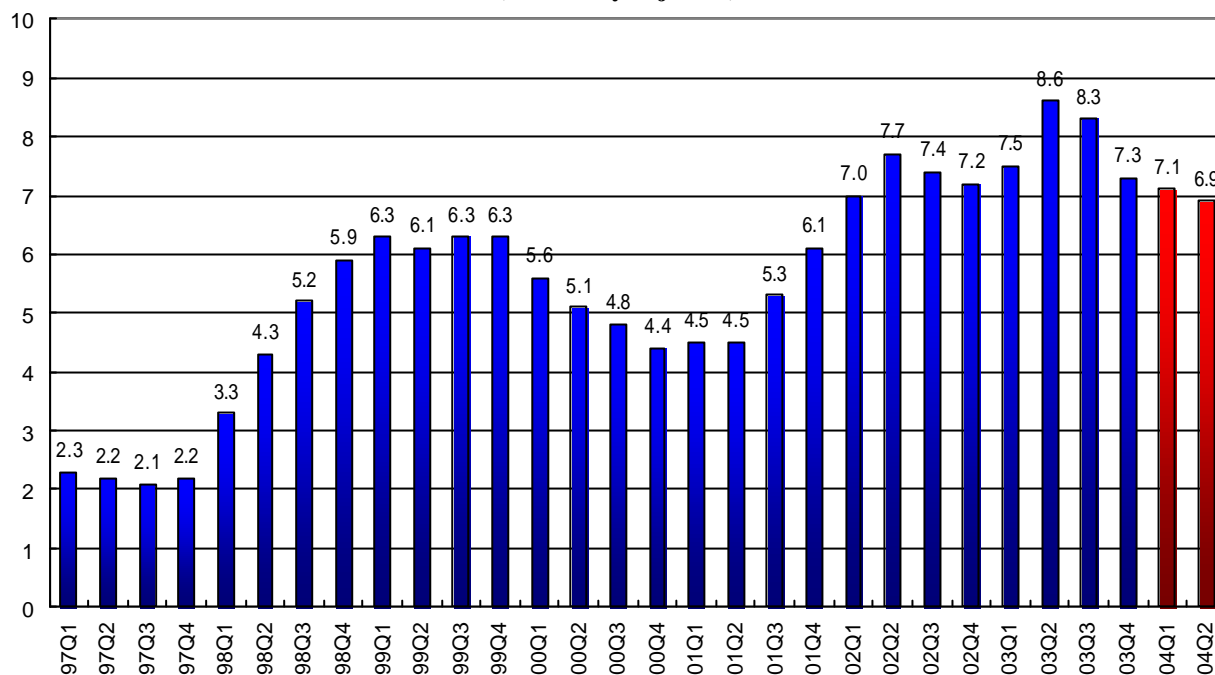
- Investment in land and construction declined by 6.4% in the fourth quarter of 2003. The fall is projected to moderate, with the investment in land and construction forecasted to drop by 4.2% in the first quarter and to revert to an increase of 0.6% in the second quarter of 2004.
- Following the 10.2% increase in the fourth quarter of 2003, investment spending in machinery and equipment is forecasted to continually expand by 5.8% in the first quarter of 2004 and by 12.1% in the second quarter of 2004 on a year-on-year basis. The accelerated growth in the second quarter is mainly due to the lower base of comparison.

**Composite Consumer Price Index**  
(Year-on-year percentage change)



- The prices of imported goods have started to increase as a consequence of the weak US dollar, thus exerting upward pressure to the general price level. Coupled with improving local demand underpinned by rising consumption and investment demand, deflation will continue to improve. In February, the composite CPI declined by 2.0%, with housing down by 2.3%, food by 0.2% and miscellaneous service by 0.5%. Deflation is forecast to be 1.9% in the first quarter of 2004 and 1.7% in the second quarter of 2004.

## Unemployment Rate (Seasonally adjusted)



- For the period from December 2003 to February 2004, the provisional seasonally adjusted unemployment rate dropped moderately to 7.2% from 7.3% in November 2003 to January 2004. The median duration of unemployment increased from 90 days in the third quarter to 109 days in the fourth quarter of 2003, thus reflecting the tough job market conditions. The unemployment level is expected to fall slowly, with the unemployment rate forecasted to be 7.1% in the first quarter of 2004 and 6.9% in the second quarter of 2004.

### Concluding Remarks

Hong Kong's economic growth since the third quarter of last year has been sustained by robust growth in the exports of goods and services, as well as by a revival in private domestic demand. Given the favorable external environment, and barring any major revision in the asset markets, the growth momentum is expected to continue. But even if the economy stayed on its growth track, it would still take one to two year for the employment situation to improve substantially. The economy is recovering, but not yet booming.

## **About Hong Kong Macroeconomic Forecast Project**

The Hong Kong Macroeconomic Forecast is based on research conducted by the APEC Study Centre of the HKU's Faculty of Business and Economics. It aims to provide the community with timely information useful for tracking the short-term fluctuations of the economy. The current quarter macro forecasts have been released on a quarterly basis since 1999.

The high frequency forecasting system was originally developed in collaboration with Professor Lawrence Klein of the University of Pennsylvania in 1999-2000. Since then, the system has been maintained and further refined by the HKU APEC Study Centre.

The project is sponsored by the HKU Foundation for Educational Development and Research. The Steering Committee is chaired by Dr Chow Yei-Ching, Chairman & Managing Director of Chevalier International Holdings Ltd, with Mr Michael Leung, Executive Chairman of Onwel Group, as Deputy Chairman. Both Dr Chow and Mr Leung are members of the Board of Directors of the HKU Foundation.

The Hong Kong Centre for Economic Research at HKU provides administrative support to the project. Researchers at the APEC Study Center are solely responsible for the accuracy and interpretation of the forecasts. Our quarterly forecasts can be accessed at <http://www.hku.hk/apec/cqm/>

**High Frequency Macroeconomic Forecasts**  
**APEC Study Center**  
**The University of Hong Kong**

Table 1: Current Quarter Model Forecast  
(Million of 2000 Dollar)

	2003					2004	
	Q1	Q2	Q3	Q4	Annual	Q1 (forecast)	Q2 (forecast)
Gross Domestic Product	323,628	316,363	356,666	370,951	1,367,608	339,439	345,416
Private Consumption Expenditure	186,673	185,538	193,521	199,937	765,669	196,220	196,869
Government Consumption Expenditure	34,313	31,264	33,264	34,178	133,019	34,828	31,733
Domestic Exports of Goods	28,470	31,416	38,419	35,505	133,810	27,494	31,117
Re-exports of Goods	380,121	419,908	467,819	485,101	1,752,949	435,068	472,361
Imports of Goods	432,701	468,962	515,205	542,735	1,959,603	496,837	531,628
Exports of Services	89,192	72,766	103,388	114,003	379,349	98,053	98,997
Imports of Services	47,171	37,060	52,202	50,804	187,237	49,826	47,295
Investment in Land & Construction	40,147	37,915	39,905	38,128	156,095	38,461	38,144
Investment in Machinery, Equip. & Computer Software	41,863	41,947	49,599	51,243	184,652	44,296	47,021
Changes in Inventories	2,721	1,631	-1,842	6,395	8,905	11,681	8,097
Date of Forecast: March 30, 2004.							

**High Frequency Macroeconomic Forecasts**  
**APEC Study Center**  
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Table 2: Current Quarter Model Forecast  
Year-on-Year Growth Rate (%)

	2003					2004	
	Q1	Q2	Q3	Q4	Annual	Q1 (forecast)	Q2 (forecast)
Gross Domestic Product	4.5	-0.5	4.0	5.0	3.3	4.9	9.2
Private Consumption Expenditure	-1.8	-3.5	1.6	3.6	0.0	5.1	6.1
Government Consumption Expenditure	1.3	0.4	0.5	5.6	1.9	1.5	1.5
Domestic Exports of Goods	-12.0	-12.6	-5.2	-0.2	-7.3	-3.4	-1.0
Re-exports of Goods	22.3	17.0	11.5	16.0	16.3	14.5	12.5
Imports of Goods	18.8	10.9	8.2	15.7	13.1	14.8	13.4
Exports of Services	12.7	-12.0	7.8	11.8	5.5	9.9	36.0
Imports of Services	-3.9	-19.6	0.5	4.2	-4.4	5.6	27.6
Investment in Land & Construction	-4.1	-9.5	-6.6	-6.4	-6.6	-4.2	0.6
Investment in Machinery, Equip. & Computer Software	11.9	-2.0	4.9	10.2	6.1	5.8	12.1
GDP Deflator Growth Rate	-4.6	-5.4	-5.7	-4.8	-5.1	-3.8	-3.3
CPI (Composite) Inflation Rate	-2.0	-2.5	-3.6	-2.3	-2.6	-1.9	-1.7
Unemployment Rate	7.5	8.6	8.3	7.3	7.9	7.1	6.9

Date of Forecast: March 30, 2004.

# High Frequency Macroeconomic Forecasts

## APEC Study Center

### The University of Hong Kong

Table 3: Selected Monthly Indicators  
Year-on-Year Growth Rate (%)

	2003						2004					
	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN
Unit Value Trade Index (Domestic Exports)	0.5	0.6	-0.2	-0.3	-1.4	-0.8	-0.8	-0.5	-1.4	-1.1	-1.0	-1.1
Unit Value Trade Index (Imports of Foodstuffs)	-0.9	0.4	0.8	1.1	2.3	3.7	3.6	3.7	4.6	4.1	4.0	3.5
Unit Value Trade Index (Imports of Consumer Goods)	0.8	0.4	0.5	0.4	0.9	1.3	0.6	0.7	0.8	0.8	1.1	1.0
Unit Value Trade Index (Imports of Raw Materials & Semi-Manufactures)	0.3	1.1	1.1	0.9	2.0	2.8	3.0	3.6	3.0	3.6	4.2	4.7
Unit Value Trade Index (Imports of Fuels)	8.9	10.0	1.8	1.8	10.5	5.6	9.6	6.2	6.5	13.6	23.4	24.1
Unit Value Trade Index (Imports of Capital Goods)	-5.1	-6.0	-5.9	-5.2	-4.9	-5.2	-4.8	-4.6	-3.4	-2.5	-2.7	-1.5
Real Retained Imports of Foodstuffs	-6.7	3.9	3.0	9.5	19.8	10.8	3.4	32.0	8.9	21.6	29.8	26.2
Real Retained Imports of Consumer Goods	0.8	-0.4	3.0	11.0	-4.4	13.2	-58.4	40.4	6.8	-3.5	8.0	3.7
Real Retained Imports of Raw Materials & Semi-Manufactures	-10.4	-6.9	-40.4	21.0	25.6	12.0	35.5	29.8	5.4	24.3	36.0	13.9
Real Retained Imports of Fuels	-6.6	-11.2	17.0	-10.2	13.6	-0.6	23.6	25.1	5.5	36.2	21.4	46.3
Real Retained Imports of Capital Goods	-3.4	3.8	12.7	-15.8	28.9	32.1	2.4	48.1	12.0	56.1	18.9	34.0
Total Motor Vehicles Newly Registered	-30.4	-40.6	-21.4	-16.9	-21.2	-3.3	-28.5	-24.9	8.2	4.3	11.2	-2.5
Private Cars Newly Registered	-28.9	-39.0	-25.6	-17.8	-20.8	-7.8	-25.1	-21.0	2.1	2.1	3.3	-3.8
Volume Index of Retail Sales	-0.3	3.0	1.1	4.6	5.1	5.7	2.9	8.6	6.6	13.0	11.7	10.1
Money Supply (M2)	4.3	4.9	5.8	8.0	6.6	8.4	10.6	11.1	13.4	14.3	14.4	15.6
Loans and Advances	-4.8	-4.5	-3.8	-0.7	-2.7	-2.0	0.9	0.5	1.1	2.6	1.7	1.5
Visitors Arrivals	-5.6	9.6	7.9	7.0	7.3	7.4	32.6	20.7	26.4	273.1	309.3	112.5
Hong Kong Resident Departures	-4.2	2.3	3.1	0.5	0.9	3.1	2.0	-1.4	15.3	47.3	26.8	12.4
Electricity Consumption	1.3	6.2	7.4	12.7	-0.2	9.4	3.6	2.8	3.8	8.1	2.6	8.3
Gas Consumption	1.4	2.5	0.9	-3.4	-0.4	2.5	1.2	2.8	0.2	3.4	4.7	1.2
Land Considerations	-22.5	11.9	3.3	37.7	60.4	40.9	34.6	93.6	75.5	65.9	103.0	117.2
Effective Exchange Rate Index	-1.5	-1.6	-2.3	-3.6	-3.2	-3.5	-3.1	-3.4	-3.4	-3.6	-2.4	-2.2

Date of Forecast: March 30, 2004.