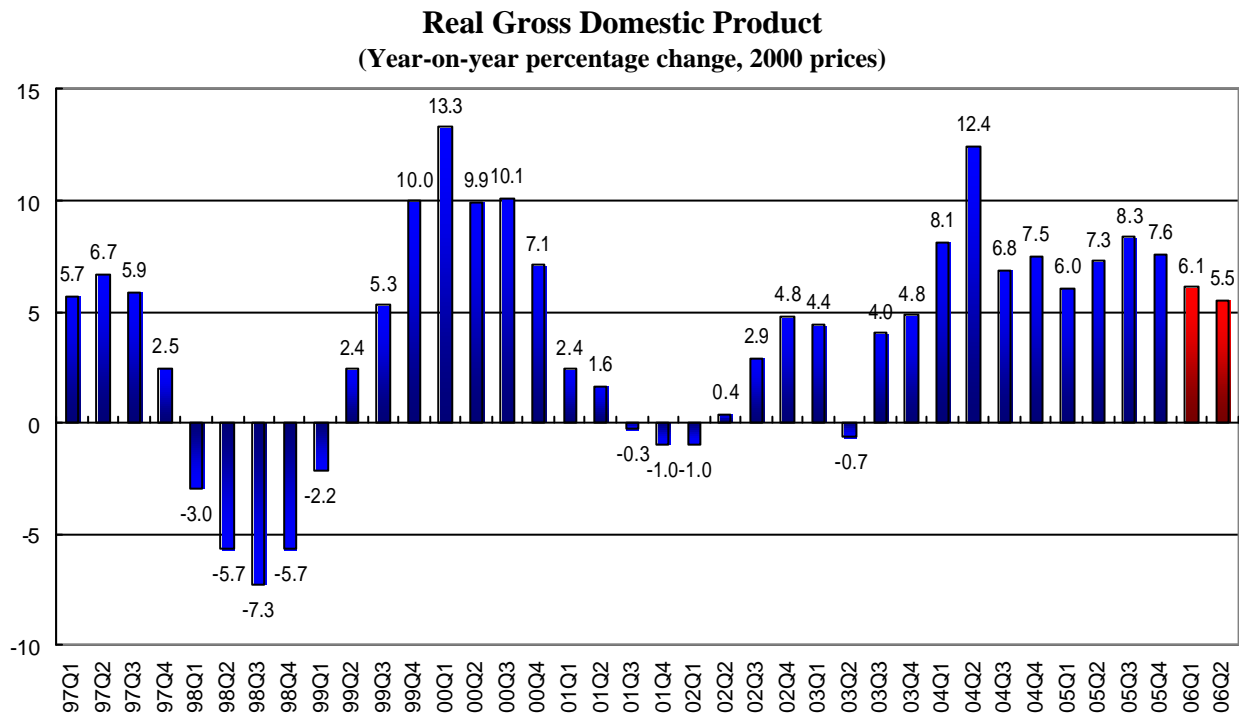


# High Frequency Macroeconomic Forecasts Current Quarter Model: 2006Q2

APEC Study Center  
The University of Hong Kong

April 6, 2006

## Stable Growth in 2006



According to the High Frequency Macroeconomic Forecast released by the APEC Study Center of The University of Hong Kong, real GDP growth in the first quarter of 2006 is estimated to be 6.1% when compared with the same period last year. This growth estimate is a slight downward revision from the 6.2% forecast released on January 4, 2006.

"In the second quarter of 2006, real GDP is forecast to grow at 5.5% on a year-on-year basis. The deceleration in real GDP growth can be attributed primarily by a slight weakening in external demand. Rising interest rates are also weighing down consumption and investment spending in the local economy," said Dr Alan Siu, Executive Director of the APEC Study Center at the University of Hong Kong.

Professor Y.C. Richard Wong, Deputy Vice-Chancellor of HKU, said, "Following the broad-based economic recovery in recent years with real GDP growing by 8.6% in 2004 and 7.3% in 2005, the Hong Kong economy will remain strong in the current year, as global economic growth is expected to continue, albeit at a slower rate. The labour market will continue to improve with the unemployment rate expected to be around 5%. Rising interest rates, wages and rentals are putting upward pressure on prices, with the inflation projected to be around 2% in the current quarter."

The forecast details are in Table 1 and Table 2, and the forecasts of selected monthly indicators are in Table 3. All growth rates reported are on a year-on-year basis.

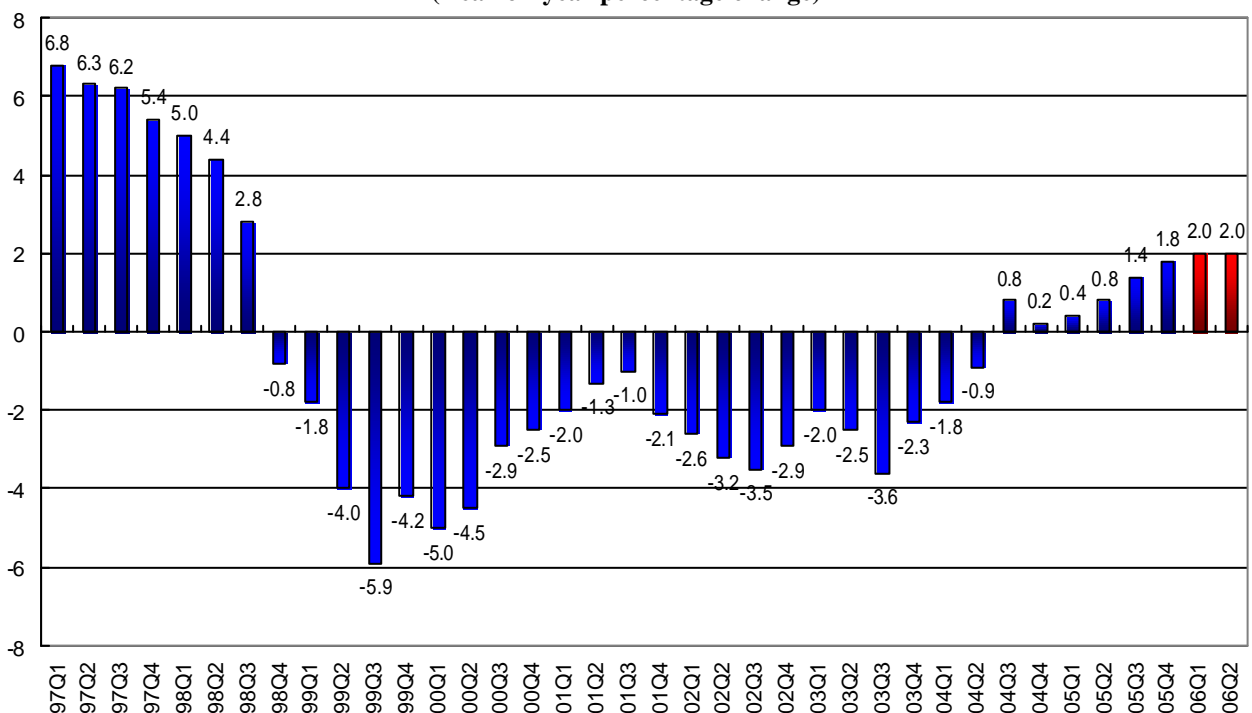
## Forecast Highlights

The highlights of our current forecasts are:

- Private consumption grew by 3.7% in the fourth quarter of 2005. Supported by continued improvement in the labour market, private consumption spending is forecast to grow by 2.5% in the first quarter of 2006 and 2.1% in the second quarter of 2006.
- The volume of retail sales grew by 10.5% in January 2006. Due to the continued strengthening of local demand and the influx of the Mainland visitors, the volume of retail sales is forecast to grow by 7.1% in the first quarter of 2006. The growth in the volume of retail sales will moderate to 5.6% in the current quarter.
- In real terms, total exports of goods rose by 11.4% in fourth quarter of 2005. It is projected to grow by 11.6% in the first quarter of 2006. In the second quarter, export growth will moderate to 9.7% reflecting a deceleration in external demand.
- Domestic Exports rose by 28.0% in the fourth quarter of 2005, picking up from the 14.2% growth in the third quarter of 2005. Hong Kong's clothing and office equipment domestic exports performed exceptionally well early this year. Taking first 2 months of 2006 together, these 2 categories accounted for 38 percentage point to the 41.7% overall nominal growth. Real domestic exports is forecast to surge by 45.3% and 33.2% in the first and second quarter of 2006, respectively.
- Re-exports grew by 10.3% in the fourth quarter of 2005. The growth in re-exports is expected to slowdown to 9.8% in the first quarter of 2006 and to 8.5% in the second quarter of 2006.
- Imports of goods grew by 12.0% in the fourth quarter of 2005, picking up from the 11.0% rate in the third quarter of 2005. The growth of imports of goods is expected to moderate to 11.0% in the first quarter, and to 9.7% in the current quarter.
- Service exports grew by 7.7% in the fourth quarter of 2005. Visitor arrival grew by 10.9% in February with visitors from the mainland accounted for 52.9% of the total growth. Service exports is forecast to grow by 6.2% and 3.7% in the first and second quarter of 2006, respectively.

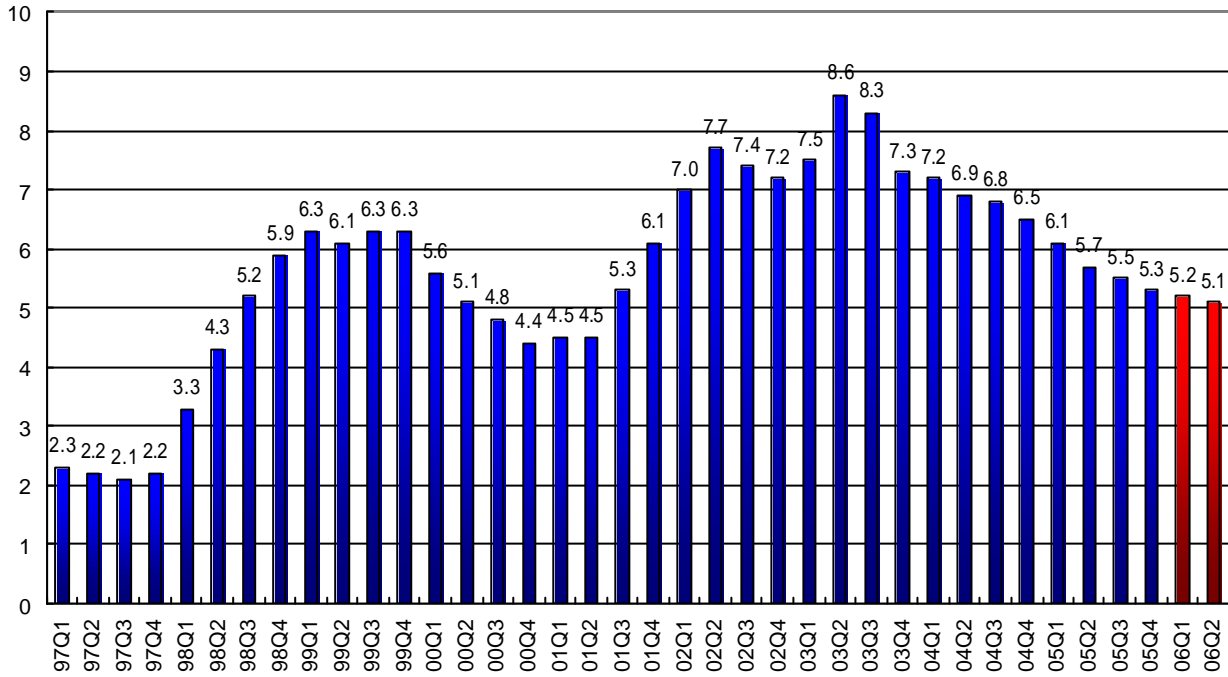
- Service imports rose by 1.4% in the fourth quarter of 2005. Transportation and travel related service imports are hit by higher energy supplement costs. Service imports is forecast to further slowdown to 0.9% and 1.8% in the first and second quarter of 2006, respectively.
- The trade balance, as measured by the net exports of goods and services, is estimated to be 19.0% of GDP in the fourth quarter of 2005, and forecast to be 15.2% of GDP in the first quarter of 2006, and 13.5% of GDP in the current quarter.
- Gross fixed capital spending grew by 7.5% in the last quarter of 2005. The investment growth is expected to moderate in the first quarter of 2006 to 4.3% and to 2.5% in the second quarter of 2006.
- Investment in land and construction dropped by 15.5% in the fourth quarter of 2005. Due to the lack of commencement of large-scale construction projects, the investment in land and construction is forecast to remain subdued and decreased by 12.0% in the first quarter of 2006 and by 11.4% in the second quarter of 2006.
- Investment spending in machinery, equipment and computer software surged by 24.2% in the fourth quarter of 2005. It is estimated to expand by 16.5% in the first quarter of 2006 and by 10.5% in the current quarter.

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



- Housing rents contributed 0.9 percentage point to the 1.6% increase in the Composite CPI in the February 2005. Increasing rentals and rising interest rates put upward pressure on the general price level. Inflation rate is forecast to increase to 2.0% in the first and second quarter of 2006.

**Unemployment Rate**  
(Seasonally adjusted)



- The provisional seasonally adjusted unemployment rate stood at 5.2% in the three months average ending in Feb 2006, same as its previous estimate in Jan 2006. The improvement in the labour market is expected to continue, with unemployment rate forecasted to be 5.2% in the first quarter of 2006 and dropping to 5.1% in the current quarter.

## Concluding Remarks

Hong Kong is expected to continue to have another year of stable economic growth, with real GDP forecast to grow by 5% to 6% for the year as a whole. But inflationary pressure is building up, and the economic outlook is still clouded by uncertainties over the interest rate cycle. Global economic growth can be derailed by unexpected sharp rises in interest rates.

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

The Hong Kong Macroeconomic Forecast is based on research conducted by the APEC Study Center 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 Center.

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/>

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

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

	2005					2006	
	Q1	Q2	Q3	Q4	Annual	Q1 (forecast)	Q2 (forecast)
Gross Domestic Product	377,691	387,747	419,905	435,562	1,620,905	400,830	409,109
Private Consumption Expenditure	208,919	214,097	214,340	225,079	862,435	214,039	218,576
Government Consumption Expenditure	34,515	30,614	32,337	32,489	129,955	34,688	30,767
Total Export of Goods	630,504	711,823	795,123	793,333	2,930,783	697,373	773,931
Domestic Export of Goods	25,938	30,251	43,607	47,576	147,372	37,680	40,308
Re-export of Goods	486,088	564,583	614,776	605,525	2,270,972	533,922	612,312
Import of Goods	522,364	603,790	653,217	650,329	2,429,700	579,735	662,507
Export of Services	118,478	116,989	136,740	140,232	512,439	125,771	121,311
Import of Services	56,211	55,164	63,457	60,224	235,056	56,727	56,150
Gross Fixed Capital Formation	86,838	92,599	93,914	94,275	367,626	90,587	103,817
GFCF in Land & Construction	37,097	33,715	33,861	31,261	135,934	32,646	29,880
GFCF in Machinery & Equip.	49,741	58,884	60,053	63,014	231,692	57,941	65,068
Changes in Inventories	-4,510	-12,432	865	939	-15,138	605	676

Date of Forecast: March 29, 2006

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Table 2: Current Quarter Model Forecast  
Year-on-Year Growth Rate (%)

	2005					2006	
	Q1	Q2	Q3	Q4	Annual	Q1 (forecast)	Q2 (forecast)
Gross Domestic Product	6.8	7.3	8.3	7.6	7.5	6.1	5.5
Private Consumption Expenditure	5.1	2.7	4.1	3.7	3.9	2.5	2.1
Government Consumption Expenditure	-4.6	-2.3	-1.6	-3.4	-3.0	0.5	0.5
Total Export of Goods	9.0	11.1	12.8	11.4	11.2	11.6	9.7
Domestic Export of Goods	-9.6	-8.3	14.2	28.0	7.6	45.3	33.2
Re-export of Goods	10.2	12.3	12.7	10.3	11.4	9.8	8.5
Import of Goods	3.8	7.0	11.0	12.0	8.6	11.0	9.7
Export of Services	11.0	8.8	8.7	7.7	8.9	6.2	3.7
Import of Services	9.4	0.3	3.8	1.4	3.6	0.9	1.8
Gross Investment	0.0	4.9	2.8	7.5	3.8	4.3	2.5
GFCF in Land & Construction	-0.1	-4.0	-4.0	-15.5	-5.9	-12.0	-11.4
GFCF in Machinery, Equip. & Computer Software	0.2	10.7	7.1	24.2	10.5	16.5	10.5
GDP Deflator Growth Rate	-2.5	-0.6	0.2	0.4	-0.5	0.9	0.8
CPI (Composite) Inflation Rate	0.4	0.8	1.4	1.8	1.1	2.0	2.0
Unemployment Rate	6.1	5.7	5.5	5.3	5.7	5.2	5.1

Date of Forecast: March 29, 2006

# High Frequency Macroeconomic Forecasts

## APEC Study Center

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

	2005						2006					
	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN
Unit Value Trade Index (Domestic Exports)	2.6	0.5	0.1	-0.7	-0.3	-0.4	-2.2	-1.9	-2.7	-3.2	-2.8	-3.1
Unit Value Trade Index (Imports of Foodstuffs)	-0.3	0.2	-0.8	-0.7	-0.6	0.0	-0.2	-0.1	0.4	1.0	1.5	2.1
Unit Value Trade Index (Imports of Consumer Goods)	3.5	2.9	2.1	2.0	1.4	1.9	0.7	0.1	0.6	0.4	0.3	0.2
Unit Value Trade Index (Imports of Raw Materials & Semi-Manufactures)	2.8	1.8	1.7	1.0	2.7	0.7	1.1	1.5	1.1	1.5	1.6	1.9
Unit Value Trade Index (Imports of Fuels)	40.1	36.1	39.2	32.8	24.9	25.1	37.6	37.5	25.3	14.0	13.9	11.1
Unit Value Trade Index (Imports of Capital Goods)	-1.2	-0.9	-1.1	-1.5	-0.7	-0.1	-1.5	-1.5	-0.9	-0.8	-0.3	0.3
Real Retained Imports of Foodstuffs	11.1	23.7	-0.3	1.8	-2.2	15.2	-3.2	11.6	8.6	7.1	6.6	3.3
Real Retained Imports of Consumer Goods	-21.8	11.6	16.9	0.2	34.5	18.0	-43.0	40.2	-6.0	8.6	7.6	6.9
Real Retained Imports of Raw Materials & Semi-Manufactures	0.0	2.5	1.5	-2.9	8.4	4.5	-4.1	2.0	9.4	14.7	-8.8	-3.6
Real Retained Imports of Fuels	-0.5	-8.2	-0.5	-32.8	5.6	6.3	6.6	-0.2	-14.6	1.5	5.3	24.1
Real Retained Imports of Capital Goods	-1.6	17.9	4.7	38.7	17.7	45.5	-2.0	35.4	37.1	20.8	6.7	19.5
Total Motor Vehicles Newly Registered	-6.6	0.9	9.4	-5.1	-6.9	-22.4	-10.7	1.2	-22.0	-27.4	-21.4	-20.5
Private Cars Newly Registered	-11.1	0.6	8.6	-4.8	-11.8	-28.4	-10.5	4.0	-23.0	-27.3	-25.2	-23.5
Volume Index of Retail Sales	5.7	5.3	4.1	3.7	3.6	5.9	10.5	6.1	4.3	-2.2	1.2	4.6
Money Supply (M2)	9.7	9.7	8.6	7.1	4.4	5.1	6.8	6.9	9.7	10.8	13.5	14.0
Loans and Advances	9.8	9.4	9.2	9.7	7.1	7.3	5.2	4.7	6.9	6.3	6.1	4.4
Visitors Arrivals	3.8	2.6	5.9	6.4	5.6	5.5	15.6	10.9	12.4	6.4	7.6	20.8
Hong Kong Resident Departures	6.3	5.0	5.1	3.8	4.5	2.8	16.5	-3.3	-6.5	-1.5	2.0	3.0
Electricity Consumption	-2.6	-1.8	7.2	11.0	6.4	-0.2	-6.0	2.4	1.1	4.0	0.4	8.2
Gas Consumption	-1.1	0.4	0.2	-2.0	0.4	3.8	1.0	-0.6	-1.6	0.1	1.4	0.9

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