

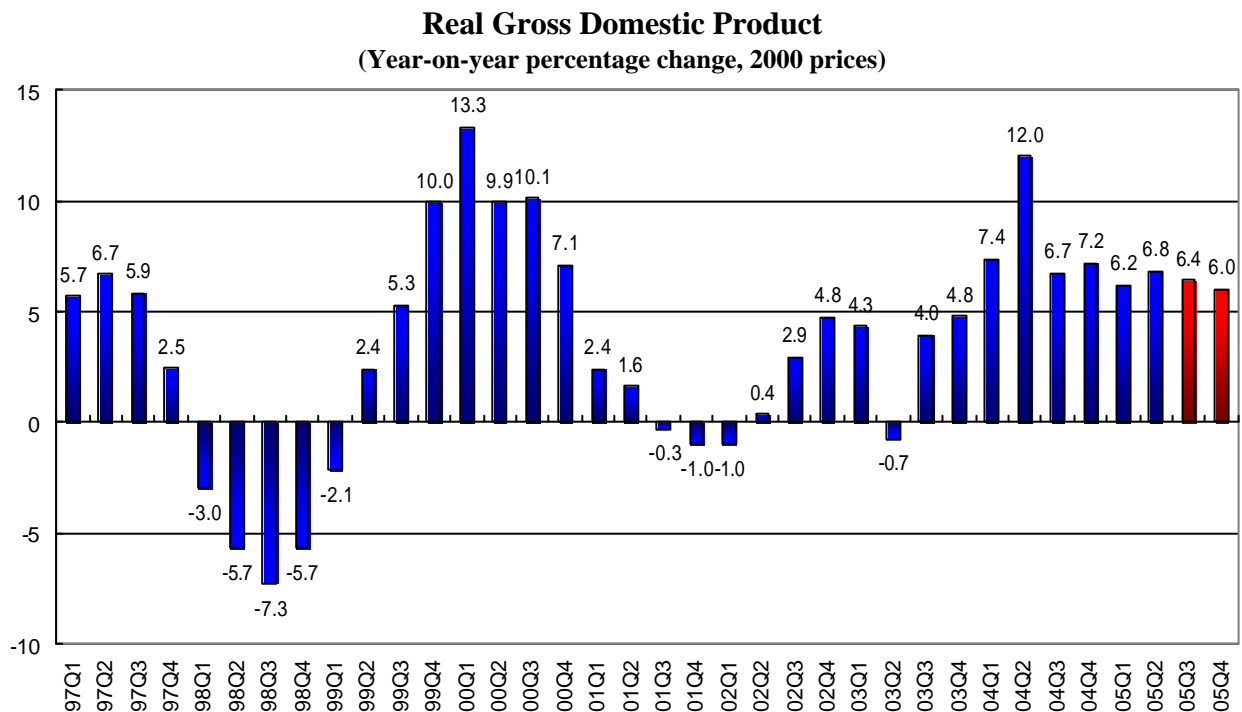


## High Frequency Macroeconomic Forecasts Current Quarter Model: 2005Q4

APEC Study Center  
The University of Hong Kong

October 5, 2005

### Hong Kong Economic Outlook



The APEC Study Center of the University of Hong Kong (HKU) released its quarterly Hong Kong Macroeconomic Forecast today. According to its High Frequency Macroeconomic Forecast, real GDP growth in Q3 of 2005 is estimated to be 6.4% on a year-on-year basis. This growth estimate is an upward revision of the 5.6% forecast released on July 7, 2005 due to stronger growth in external trade. In the fourth quarter of 2005, real GDP growth is forecast to moderate to 6.0% when compared with the same period last year.

Professor Richard Wong Yue-Chim, Director of the APEC Study Center at HKU said that, "Despite surging oil prices and tightening of monetary conditions, the expected slowdown in global economic growth has turned out to be mild. The expansion of the Hong Kong's economy since 03Q3 is expected to continue with real GDP estimated to be growing by 6.2% in the second half of this year, only a slight drop from the 6.5% growth in the first half. For the year as a whole, real GDP is likely to grow by 6.4%."

"The labour market will continue to improve, with the unemployment rate dropping to an estimated average of 5.4% in the current quarter. Rising import prices and rents will pull up consumer prices. Inflation rate is forecast to increase to 1.7% in the current quarter," according to Dr Alan Siu, Executive Director of the APEC Study Center at HKU.

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.

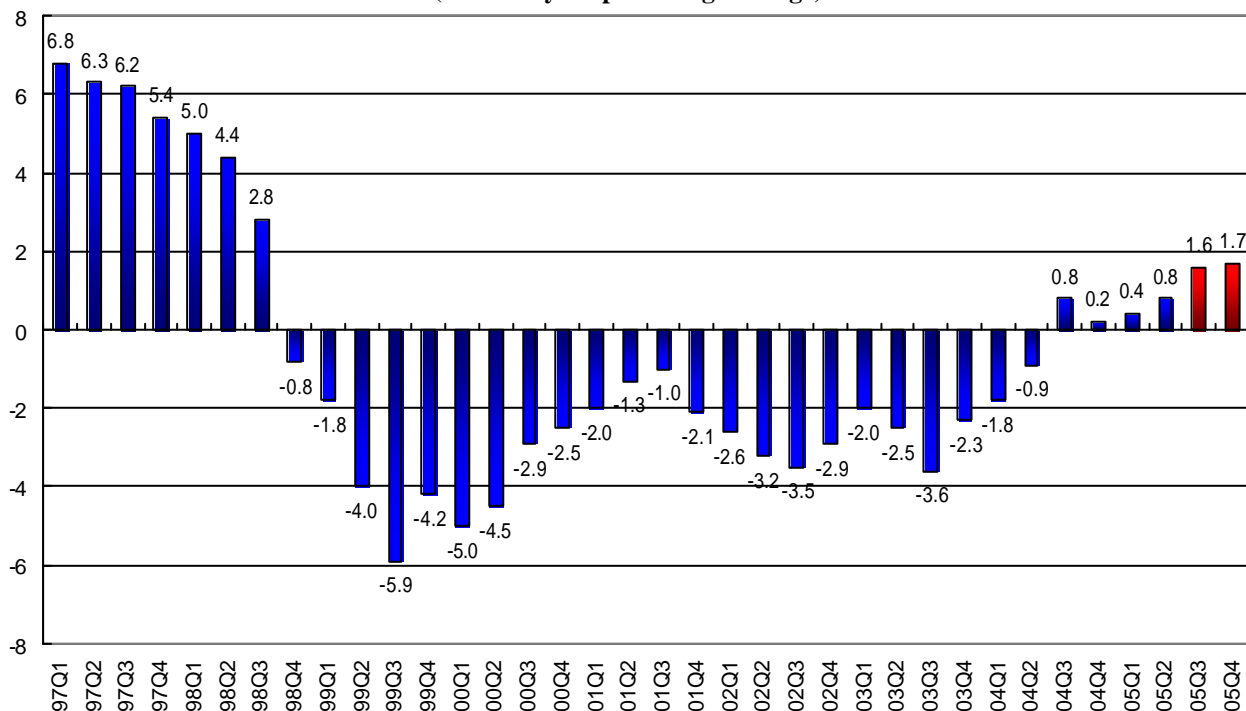
## Forecast Highlights

The highlights of our current forecasts are:

- Private consumption spending grew by a modest rate of 2.7% in Q2. Consumer sentiment continues to improve, led by the robust growth of the economy since the 03Q3, with real GDP growing continuously for more than 8 quarters. Private consumption expenditure is estimated to grow by 3.3% in Q3 and further pick up to 4.1% in Q4. For the year as a whole, private consumption spending is estimated to grow by 3.6%
- The volume of retail sales in July 2005 registered a broad-based increase of 5.6% when compared with same period last year. Clothing, footwear and allied products, consumer durable goods and other consumer goods grew at 8.2%, 4.4% and 9.6% respectively. The volume of retail sales is forecast to grow by 6.6% in Q3 and 4.4% in Q4 of 2005. For 2005 as a whole, it is expected to rise by 6.3%.
- Total exports grew by 11.1% in Q2, faster than the 9.0% growth in Q1, but is expected to moderate in the second half due to a weaker external environment. It is estimated to be 9.0% in Q3 and forecast to be 8.0% in Q4. For the year as a whole, total exports are projected to grow by 9.2% in 2005.
- After falling by 9.6% and 8.3% in Q1 and Q2 respectively, domestic exports are projected to be on its declining trend, dropping by 3.2% in Q3 and 6.4% in Q4. For the year as a whole, it is forecast to decrease by 6.6% in 2005.
- Re-exports grew by 12.3% in Q2, faster than the 10.2% increase in Q1, but is forecast to grow more slowly in the second half of this year, due to weaker external demand. It is estimated to grow by 9.8% in Q3 and moderate to 9.0% in Q4. For the year as a whole, it is projected to grow by 10.3%.
- Service exports grew by 7.8% in Q2. The number of visitor arrivals increased by 8.7% in the first 7 months of this year, when compared with the same period last year. Inbound tourism is expected to continue to perform well for the rest of this year. Service exports is forecast to expand by 6.8% and 7.0% in Q3 and Q4 of 2005 respectively. The annual growth is estimated to be 7.5% in 2005.
- Imports of goods grew by 7.0% in Q2. Fueled by the revaluation of RMB and surging oil prices, import prices have been rising for six consecutive quarters, thus dampening real import growth. The growth of imports of goods is estimated to be 7.9% in Q3 and 8.8% in the current quarter. The growth is forecast to be 7.0% for 2005.

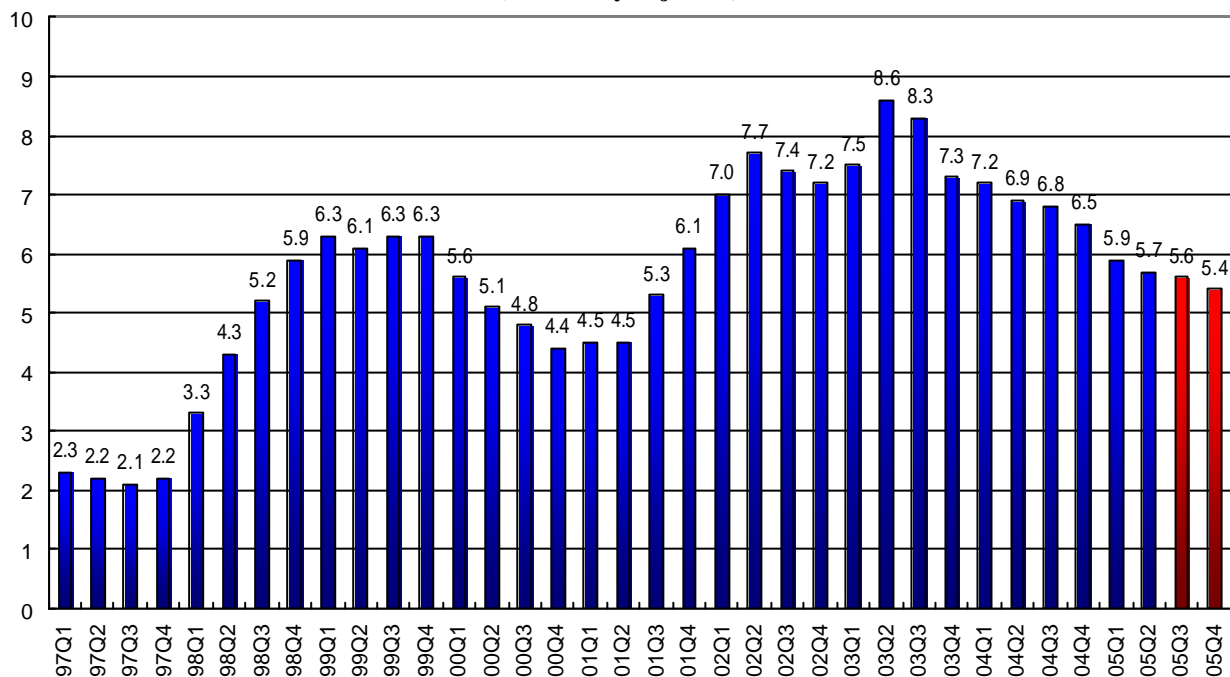
- Import of services dropped by 0.4% in Q2. The growth in travel related service imports will be dampened by rising oil prices which has made air travel more expensive. Service imports is forecast to grow by 4.5% and 5.0% in Q3 and Q4, respectively. It is estimated to grow by 3.7% in the whole year of 2005.
- The trade balance, as measured by the net exports of goods and services, is estimated to be 13.4% of GDP in Q2. It is forecast to be 17.3% of GDP in Q3 of 2005, and 18.1% of GDP in the current quarter.
- Gross fixed investment rose by 3.5% in Q2 of 2005. The growth is expected to contract by 1.9% in Q3 and 2.5% in Q4 of 2005.
- Investment in land and construction dropped by 6.6% in Q2 of 2005. Due to the lack of commencement of major projects, the investment in land and construction is forecast to drop by 2.7% in Q3 and by 4.6% in Q4 of 2005. The annual decrease of 2005 is estimated to be 3.4%.
- Investment spending in machinery, equipment and computer software surged by 10.1% in Q2 of 2005 due to delivery of several aircrafts. Underpinned by the expectation of continued economic growth, investment spending is expected to hold up in the second half of this year. It is estimated to grow by 4.8% in Q3, 7.6% in Q4 and 5.9% for the year as a whole.

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



- As predicted, inflation, as measured by the year-on-year percentage change of the Composite CPI, grew by 0.8% in Q2, accelerating from the 0.4% increase in Q1. Started in July, the housing component of the Composite CPI registered the first annual gain since the 1998 Q4. Rising rentals since 2004 Q2 has finally started to be reflected in the index. This trend will continue as old rental contracts expiring in the coming months will have to be renewed at higher rates. The CPI inflation in August edged up to 1.4% from the 1.3% in July. Rising import prices and higher energy prices also contribute to the inflationary pressure. Inflation rate is estimated to be 1.6% in Q3 and forecast to increase to 1.7% in the current quarter.

### Unemployment Rate (Seasonally adjusted)



- The provisional seasonally adjusted unemployment rate stood at 5.7% in the three months average ending in August 2005, unchanged from the previous estimate for the three months ending in July 2005. Even though the unemployment rate is still relatively high compared to the levels in the 90s, around 200,000 additional jobs have been created since the trough in 2003. In tandem with the growing economy, total employment will increase. The unemployment rate is forecast to be 5.6% in Q3 of 2005, and drop slightly to 5.4% in the current quarter, with the number of unemployed dropping by 6,000 by year end.

### Concluding Remarks

Surging oil prices is a cause for concern. Oil prices will be likely to remain high. The risk of slower global economic growth next year is now higher. Persistent high oil prices could lead to further monetary tightening in the U.S. Higher interest rates than currently expected will dampen global economic growth.

## **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/>

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

	2004			2005			
	Q3	Q4	Annual	Q1	Q2	Q3 (forecast)	Q4 (forecast)
Gross Domestic Product	387,038	403,653	1,504,147	375,461	384,557	411,844	427,871
Private Consumption Expenditure	204,595	216,406	827,093	207,506	212,899	211,421	225,309
Government Consumption Expenditure	32,848	33,611	133,961	34,447	30,606	33,012	33,779
Total Export of Goods	583,867	586,246	2,175,685	512,026	594,834	636,140	633,270
Domestic Export of Goods	38,173	37,162	137,011	25,938	30,251	36,947	34,772
Re-export of Goods	545,694	549,084	2,038,674	486,088	564,583	599,193	598,498
Import of Goods	588,404	580,680	2,236,642	522,364	603,790	634,922	631,735
Export of Services	123,442	127,153	462,428	116,112	113,289	131,822	136,089
Import of Services	59,084	57,375	220,962	54,164	52,911	61,749	60,268
Gross Investment	92,588	88,622	357,457	87,327	92,390	94,363	90,826
Investment in Land & Construction	35,497	37,308	145,458	37,304	33,008	34,537	35,608
Investment in Machinery & Equip.	57,091	51,314	211,999	50,023	59,382	59,826	55,218
Changes in Inventories	-2,814	-10,330	5,127	-5,428	-2,760	1,758	601
Date of Forecast: September 27, 2005							

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

	2004			2005				
	Q3	Q4	Annual	Q1	Q2	Q3 (forecast)	Q4 (forecast)	Annual (forecast)
Gross Domestic Product	6.7	7.2	8.2	6.2	6.8	6.4	6.0	6.4
Private Consumption Expenditure	5.2	5.8	6.8	4.4	2.7	3.3	4.1	3.6
Government Consumption Expenditure	-1.3	-1.7	0.7	-4.8	-2.3	0.5	0.5	-1.6
Total Export of Goods	15.3	12.6	15.3	9.0	11.1	9.0	8.0	9.2
Domestic Export of Goods	-0.6	4.7	2.4	-9.6	-8.3	-3.2	-6.4	-6.6
Re-export of Goods	16.6	13.2	16.3	10.2	12.3	9.8	9.0	10.3
Import of Goods	14.2	7.0	14.1	3.8	7.0	7.9	8.8	7.0
Export of Services	12.2	7.7	15.3	8.8	7.8	6.8	7.0	7.5
Import of Services	7.2	6.1	11.5	5.4	-0.4	4.5	5.0	3.7
Gross Investment	2.1	-1.4	4.1	0.4	3.5	1.9	2.5	2.1
Investment in Land & Construction	-10.4	-0.5	-6.0	0.0	-6.6	-2.7	-4.6	-3.4
Investment in Machinery & Equip.	11.9	-2.1	12.4	0.7	10.1	4.8	7.6	5.9
GDP Deflator Growth Rate	-2.9	-2.6	-3.3	-2.2	-1.0	-0.1	0.6	-0.5
CPI (Composite) Inflation Rate	0.8	0.2	-0.4	0.4	0.8	1.6	1.7	1.1
Unemployment Rate	6.8	6.5	6.9	6.1	5.7	5.6	5.4	5.7

Date of Forecast: September 27, 2005

# High Frequency Macroeconomic Forecasts

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

	2005											
	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
Unit Value Trade Index (Domestic Exports)	5.1	4.2	4.9	4.9	4.1	5.1	2.6	1.7	0.9	0.0	0.0	-0.8
Unit Value Trade Index (Imports of Foodstuffs)	3.1	2.8	2.4	2.2	1.6	0.5	-0.3	-0.5	-1.6	-1.8	-1.8	-1.7
Unit Value Trade Index (Imports of Consumer Goods)	2.8	3.3	3.7	3.9	3.7	3.2	3.4	2.9	2.8	3.3	2.9	3.1
Unit Value Trade Index (Imports of Raw Materials & Semi-Manufactures)	6.6	6.1	4.9	4.1	3.7	3.2	2.8	2.4	1.8	1.5	1.2	1.3
Unit Value Trade Index (Imports of Fuels)	19.6	24.7	36.9	42.3	37.3	40.5	40.1	33.2	30.7	23.6	23.4	32.2
Unit Value Trade Index (Imports of Capital Goods)	1.5	0.5	0.0	-0.3	-0.3	-0.7	-1.3	-1.1	-0.5	-0.7	-0.5	-0.2
Real Retained Imports of Foodstuffs	1.1	-0.6	1.2	2.3	2.0	1.3	-0.4	-0.5	0.4	-1.2	0.2	-0.4
Real Retained Imports of Consumer Goods	1.4	1.6	1.7	1.2	2.0	2.5	2.2	2.1	2.2	2.2	2.7	2.8
Real Retained Imports of Raw Materials & Semi-Manufactures	3.4	3.7	2.6	1.7	1.6	0.4	0.7	0.9	0.5	0.0	-0.2	-0.1
Real Retained Imports of Fuels	17.2	23.1	35.5	49.9	45.4	42.1	42.9	38.2	36.8	29.8	24.3	36.1
Real Retained Imports of Capital Goods	2.5	0.9	0.0	2.3	1.8	0.7	0.3	0.3	0.2	0.8	1.2	0.7
Total Motor Vehicles Newly Registered	11.6	-17.8	-5.9	18.5	7.0	-5.9	-6.6	0.6	2.9	-3.3	-10.9	-5.5
Private Cars Newly Registered	6.0	-18.6	-10.7	6.1	6.5	-2.6	-11.1	-5.9	-2.0	-5.9	-14.7	-4.4
Volume Index of Retail Sales	3.0	16.0	5.2	7.8	6.4	5.2	5.6	7.4	6.7	4.7	4.8	3.8
Money Supply (M2)	6.5	7.0	9.2	9.9	8.5	8.9	9.7	10.3	9.8	8.7	6.1	6.7
Loans and Advances	5.2	4.1	6.8	7.8	8.3	8.7	9.8	10.1	9.2	9.2	6.4	6.5
Visitors Arrivals	8.3	20.0	5.7	11.9	7.5	5.8	3.8	6.9	13.4	9.7	11.2	11.6
Hong Kong Resident Departures	-1.2	16.7	15.0	-4.0	6.0	2.5	6.3	10.9	3.8	4.5	7.4	4.8
Electricity Consumption	12.5	6.0	10.5	6.6	17.5	-1.8	-2.6	-1.8	-0.9	5.8	-5.2	-7.7
Gas Consumption	0.3	1.6	1.0	1.1	0.0	-1.0	-1.1	0.4	1.2	2.1	1.3	3.3

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