

High-Frequency Macro Forecasts: 4th Quarter 2000

<http://www.hku.hk/apec/cqm/00Q4/>

Growth at Slower Pace

Following the hefty economic growth in the first half of this year, with real GDP growing at 14.3% in the first quarter and 10.8% in the second quarter, output growth will moderate in the second half. According to the High-Frequency Macroeconomic Forecasting Model of the APEC Study Center of The University of Hong Kong, real GDP growth in the third quarter is estimated to be 7.9% on a year-on-year basis, and is forecasted to grow at 4.5% in the fourth quarter. For the year as a whole, real GDP is projected to grow by 9.1%.

Our Mistakes

In our previous release on July 3, we predicted real GDP growth to be 11.8% and 11.0% in the second and third quarter, respectively. Compared with the official figure of 10.8% in the second quarter, we were off by 1 percentage point. The major differences between our forecasts and the official estimates are in private consumption spending and domestic exports which grew more slowly than were predicted by our model. Information released in the past two months confirms the slower growth in consumption and domestic exports. Accordingly, our forecasts for the third and fourth quarters are revised downward.

Consumption

Private consumption spending grew by 8.8% and 5.2% in the first and second quarter, respectively, and is expected to weaken. The growth in the third quarter is estimated to be 4.4%, and decreases to 2.8% in the fourth quarter. The weakening in consumption spending reflects the slow down in economic growth, and an increase in the saving rate. Consumption spending has been growing at substantially slower rates than real GDP in the past four quarters. This implies that households are saving more and are in the process of rebuilding their financial portfolios. The consumption to output ratio is now estimated to be at a historically low value of 0.54. The normal figure is around 0.60. With continued growth in the economy, private consumption spending is expected to pick up next year.

Retail Sales

Retail prices for major sectors remain weak, and the fall in prices is the main factor for the growth in the volume in retail sales. The retail price of clothing, footwear and allied products dropped by about 11% and their volume grew by 24.5% in July 2000 compared to a year ago.

External Trade

The growth in external trade is expected to be moderate. One factor is that export prices have started to increase in June. The surge in oil prices will hurt the growth in Europe and the U.S. Also, the recovery of the regional trade has now been completed. Re-export trade is expected to have double-digit growth, with 14.4% in the third quarter and 13.0% in the fourth. Domestic export of goods is expected to grow at 6.5% and 4.9% in the third and fourth quarter respectively.

External trade is the life blood of the economy. As a ratio of GDP, the export of goods increased from around 1 in 1990 to an estimated 1.87 in 00Q4, while the import of goods jumped from around 1 in 1990 to an estimated to 1.93 in 00Q4.

Exports minus Imports

	Visible	Invisible	Total
00Q1	-0.08	0.11	0.03
00Q2	-0.08	0.12	0.04
00Q3	-0.04	0.13	0.08
00Q4	-0.06	0.14	0.08

Investment

The strong growth of investment spending in machinery and equipment, growing by 19.6% in the second quarter of 2000, is expected to continue. The rates are estimated at 14.2% and 11.0% in the third and fourth quarter respectively. Investment in machinery and equipment will account for around 16% of GDP in the second half of this year.

The outlook on land and construction is positive. The rate of decline is estimated to be 7.7% and 5.8% in third and fourth quarter respectively. The investment on land and construction will account for around 11% of GDP in the second half of this year, a substantial drop from the 18% figure in 1997Q1.

Property Market

The property market is showing signs of recovery. Rental and capital values have stabilized since 1999Q4. The number and the value of transaction started to grow again in the third quarter.

Consumer Prices

We are still in a deflationary environment. As there was a 50% rebate on rates in the third quarter of last year, with a lower base of comparison, the deflation rate is estimated to be 3.0% in the third quarter of 2000. The deflation rate is forecasted to be 4.2% in the fourth quarter of 2000. The drop in prices is mainly concentrated in the clothing and footwear, and housing sectors. In August, these two components of the Composite CPI drop by 11.6% and 6.4% respectively. Excluding housing, the deflation rate would only be 1%, instead of the 2.7% in August.

Employment

The employment situation continues to improve. The unemployment rate is projected to be at 4.9% and 4.8% in the third and fourth quarter respectively. The unemployment is still concentrated in the construction sector with double-digit unemployment rates. From 1999Q2 to 2000Q2, the labor force increased slightly from 3.35 million to 3.38 million; and the number of employed persons increased from 3.15 million to 3.21 million. The increase in employment was thus faster than the increase in the labor force in this period.

Payroll

Table 1: Nominal Payroll Index (y-o-y Growth Rate)

99Q1	1.75
99Q2	-1.18
99Q3	-1.10
99Q4	-0.66
00Q1	0.00
00Q2	1.76

From 1994Q1 to 2000Q2, the trend growth rate of nominal payroll is estimated to be 6.6% per year.