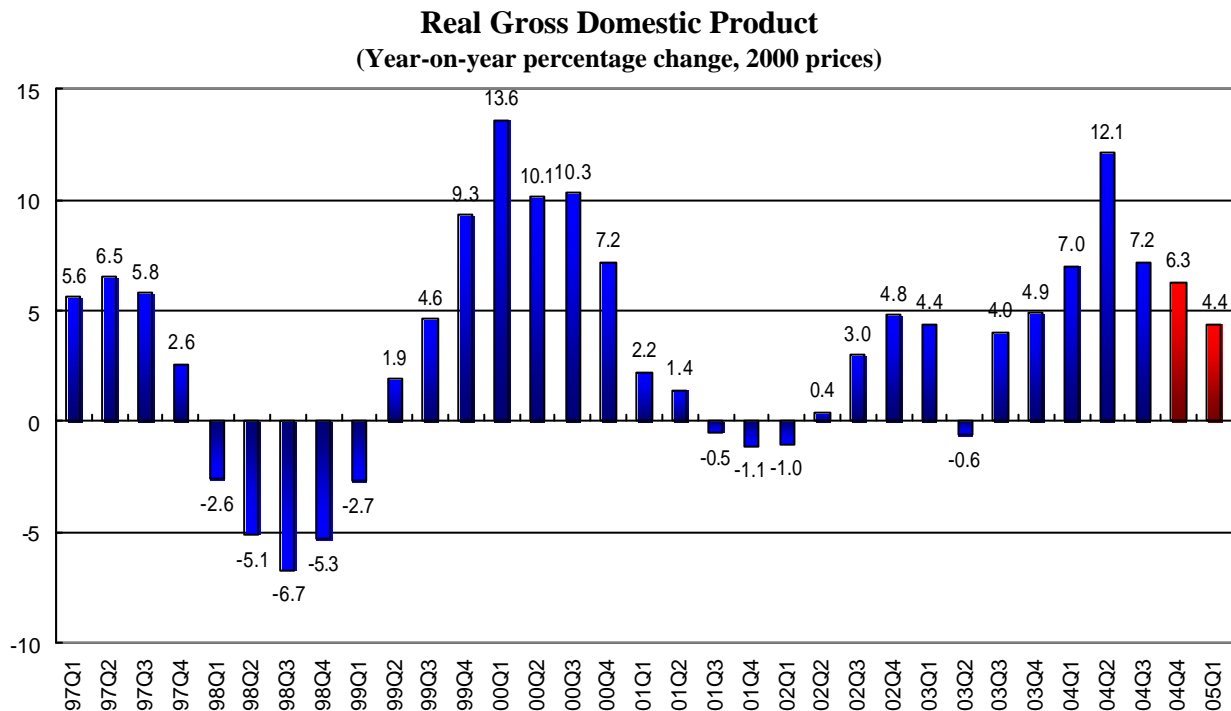


High Frequency Macroeconomic Forecasts Current Quarter Model: 2005Q1

APEC Study Center
The University of Hong Kong

January 11, 2005

Strong Economic Recovery in 2004 and Continued Growth in 2005



According to the High Frequency Macroeconomic Forecast conducted by the APEC Study Center of The University of Hong Kong, real GDP growth in the fourth quarter of 2004 is forecast to be 6.3% on a year-on-year basis. This growth estimate is an upward revision of the 3.6% forecast released on October 6, 2004 due to stronger external demand.

For the year of 2004 as a whole, the real GDP growth is estimated to be a very robust 8.0%, with the average consumer price level declining by only 0.5%, and deflation finally beaten in the third quarter of last year. "The above trend-growth in the Hong Kong economy in 2004 is excellent news. This reflects the sound fundamentals of our economy. Our external sector is very competitive and is able to capitalize on the strong global economic growth last year, particularly in the Mainland. The ending of deflation will enable business to enjoy stronger cash flows." said Dr Chow Yei-Ching, Chairman and Managing Director of Chevalier International Holdings Ltd, and Chairman of the Steering Committee of the forecasting project.

Professor Y.C. Richard Wong, Deputy Vice-Chancellor of HKU, said "On top of the favourable global economic environment, the strong output growth is also underpinned by a sharp revival in private domestic demand brought about by steady improvement in the property and stock markets. The weakening of the US dollar also helps to strengthen Hong Kong's competitiveness."

"The growth momentum is expected to moderate, with output growth forecast to grow by 4.4% in the current quarter. The slowdown reflects a weakening in external demand, as Hong Kong's major trading partners growing more slowly." said 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.

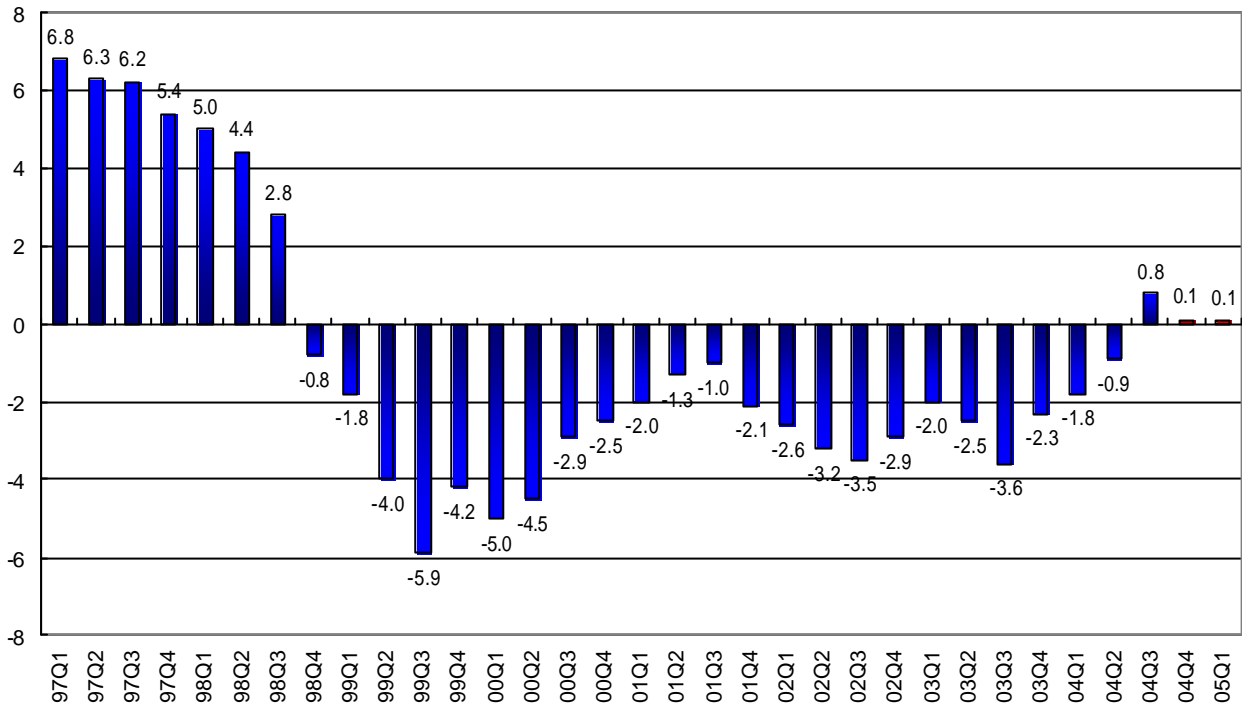
Forecast Highlights

The highlights of our current forecasts are:

- Boosted by continued economic recovery, private consumption spending rose by 5.1% in the third quarter of 2004. The strong performance both in the property and stock markets helps to improve the balance sheets of the private sector. The wealth effect will continue to underpin strong growth in consumption demand. Private consumption spending is projected to grow by 4.7% in the fourth quarter of 2004, and by 6.7% for the year of 2004 as a whole. In the first quarter of 2005, consumption is forecasted to grow by 4.3%.
- The volume of retail sales grew by 6.8% in November 2004. Buoyed by improving domestic demand and the influx of Mainland visitors, the volume of retail sales is forecast to grow by 6.4% in the fourth quarter of 2004, and by 8.9% in 2004. The growth in the volume of retail sales will moderate to 2.9% in the current quarter.
- The weakening of the US dollars enhances the competitiveness of Hong Kong's exports. Following the strong growth of 15.3% in the third quarter of 2004, total exports of goods is forecast to grow by 11.6% in the last quarter of 2004, and by 15% for the year as a whole. In the current quarter, it is projected to grow by 8.9%.
- Domestic exports recorded a decrease of 0.6% in the third quarter, reverting the increase of 5.0% in the second quarter of 2004. It is expected to rebound strongly in the fourth quarter of 2004 and in the first quarters of 2005 at 6.4% and 5.2% respectively. For the year of 2004, it is projected to grow by 2.8%.
- Re-exports grew by 16.6% in the third quarter of 2004. The double-digit growth in re-exports is expected to be maintained, growing by 12.0% in the fourth quarter of 2004, but moderating to 9.2% in the first quarter of 2005. The annual growth of 2004 is estimated to be 16.0%.

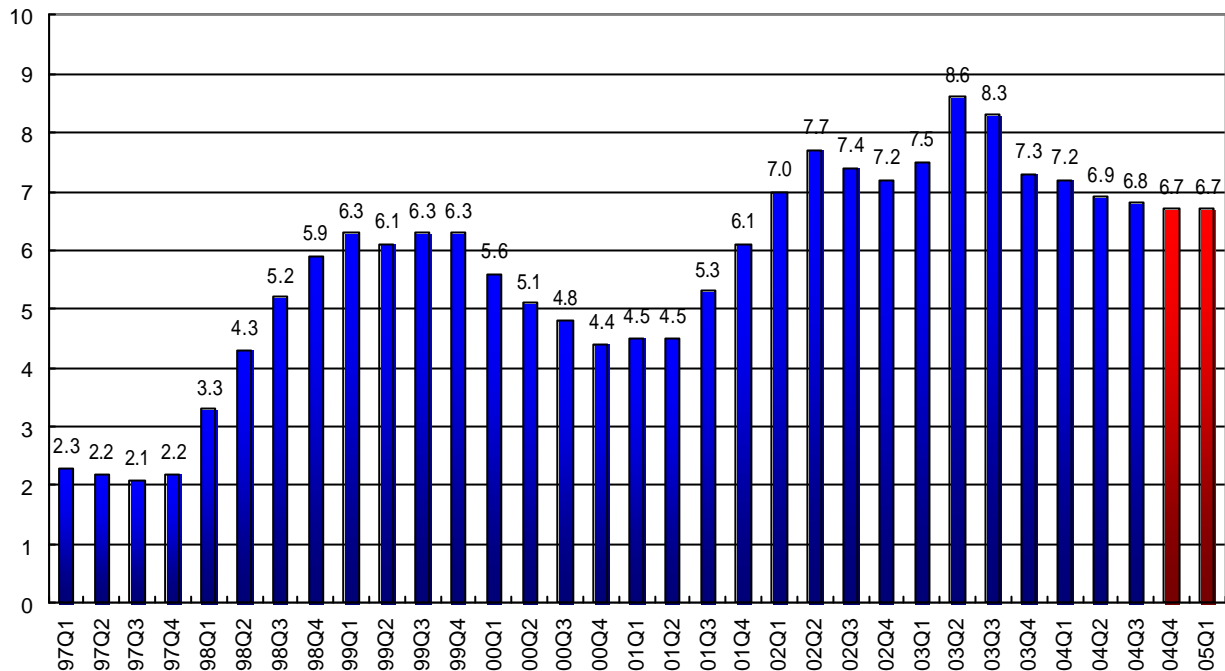
- Underpinned by the robust growth in the number of visitors from the Mainland, exports of services surged by 10.3% in the third quarter of 2004. The total number of visitor arrivals rose by 15.8%, with the hotel occupancy rate setting a historical record in the past 16 years at 96% in November 2004. The export of services is estimated to rise by 8.9% and 7.7% in the fourth quarter of 2004 and in the first quarter of 2005 respectively. For the year of 2004, the export of services is projected to grow by 14.5%.
- Imports of goods expanded by 14.2% in the third quarter of 2004. Import prices went up as a result of the weakening of the US dollar, and served to decelerate the growth of the imports of goods to 7.8% in the fourth quarter of 2004. It is forecasted to grow by 14.4% for year of 2004 as a whole. The growth of the imports of goods is expected to further moderate to 6.0% in the current quarter.
- Imports of services went up by 5.8% in the third quarter of 2004. The number of resident departures grew by 5.6% in November 2004. Service imports is projected to slow down to 1.5% in the fourth quarter of 2004, and to grow by 9.2% for the year of 2004 as a whole. The growth will pick up again to 5.7% in the first quarter 2005.
- The trade balance, as measured by the net exports of goods and services, is estimated to be 14.6% of GDP in the third quarter of 2004, and forecast to be 16.9% of GDP in the fourth quarter of 2004, and 10.7% of GDP in 2004. For the current quarter, it is projected to be 9.6% of GDP.
- Positive economic outlook, coupled with the low interest rate environment encouraged fixed capital formation in 2004. Although the investment in land and construction remained subdued, the investment in machinery and equipment registered strong growth. The total gross fixed investment rose by 4.9% in the third quarter of 2004, and is forecast to grow by 3.5% in the fourth quarter of 2004, and by 6.5% in the full year of 2004. The growth in fixed investment will moderate to 0.7% in the current quarter.
- Investment in land and construction dropped by 4.6% in the third quarter of 2004. Due to lack of commencement of major construction projects, the investment in land and construction is forecasted to drop by 3.5% in the fourth quarter of 2004 and 2.3% in the first quarter of 2005. In 2004, it is estimated to decrease by 4.2%.
- Investment spending in machinery, equipment and computer software grew by 12.2% in the third quarter of 2004. It is estimated to moderate to 8.5% in the fourth quarter of 2004 and further decelerate to a 3.0% growth in the current quarter. It is forecasted to grow by 15.2% on an annual basis in 2004.

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



- Deflation, as measured by the year-on-year percentage change of the Composite Consumer Price Index, was finally beaten in the third quarter of 2004, after 68 consecutive months of painful adjustment. Better consumer sentiment, rising import prices, revival of property prices and the influx of Mainland visitors all contributed to the 0.8% increase in the Composite CPI in the third quarter of 2004. It is forecasted to grow by 0.1% both in the fourth quarter of 2004 and the current quarter. The consumer price level is projected to decrease by a modest 0.5% on average during 2004.

Unemployment Rate (Seasonally adjusted)



- The provisional seasonally adjusted unemployment rate stayed unchanged at 6.7% in the three months average ending in November 2004 from its previous estimate for the three months ending in October 2004. The median duration of unemployment fell from 97 days in the second quarter of 2004 to 88 days in the third quarter of 2004 reflecting an improvement in the employment situation. The unemployment rate is expected to fall only slowly, and is forecasted to remain at the 6.7% level in the fourth quarter of 2004, and in the current quarter. For the whole year of 2004, the unemployment rate is estimated to average out at 6.9%.

Concluding Remarks

Dr Alan Siu said "Despite an expected increase in interest rates, and a slowing down of Hong Kong's major trading partners, with the US economy forecasted to grow at 3.6%, and the Mainland at 8.5%, the global economic environment appears to remain favourable in 2005. The Hong Kong economy is forecasted to continue its above trend-rate growth at around 6% in 2005, with consumer prices rising by 3% at year-end. Job growth will remain sluggish, with the unemployment rate declining slowly to around 6.3% by the end of this year." According to Dr. Siu, the major risk factor remains to be the volatilities induced by unexpected movements in oil prices

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

	2003			2004					2005
	Q3	Q4	Annual	Q1	Q2	Q3	Q4 (forecast)	Annual (forecast)	Q1 (forecast)
Gross Domestic Product	355,273	369,262	1,361,213	344,382	352,754	380,751	392,655	1,470,542	359,462
Private Consumption Expenditure	190,340	200,018	759,401	195,623	205,061	199,992	209,397	810,073	204,119
Government Consumption Expenditure	33,292	34,210	133,056	36,063	31,251	32,791	33,616	133,721	36,243
Total Export of Goods	506,238	520,606	1,886,759	469,964	535,608	583,867	581,115	2,170,554	511,928
Domestic Export of Goods	38,419	35,505	133,810	28,685	32,991	38,173	37,771	137,620	30,181
Re-export of Goods	467,819	485,101	1,752,949	441,279	502,617	545,694	543,344	2,032,934	481,747
Import of Goods	515,205	542,735	1,959,603	503,287	564,271	588,404	584,970	2,240,932	533,331
Export of Services	106,011	113,209	383,438	101,078	97,809	116,930	123,259	439,076	108,814
Import of Services	53,547	52,383	193,486	50,121	51,372	56,673	53,175	211,341	52,961
Gross Investment	89,892	89,237	340,842	86,669	89,652	94,273	92,381	362,975	87,295
Investment in Land & Construction	39,006	37,169	152,613	37,100	35,984	37,199	35,873	146,156	36,246
Investment in Machinery & Equip.	50,886	52,068	188,229	49,569	53,668	57,074	56,509	216,820	51,049
Changes in Inventories	-1,748	7,100	10,806	8,393	9,016	-2,025	-8,969	6,415	-2,644

Date of Forecast: January 7th, 2005

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

	2003			2004					2005
	Q3	Q4	Annual	Q1	Q2	Q3	Q4 (forecast)	Annual (forecast)	Q1 (forecast)
Gross Domestic Product	4.0	4.9	3.2	7.0	12.1	7.2	6.3	8.0	4.4
Private Consumption Expenditure	0.1	3.7	-0.9	6.0	11.2	5.1	4.7	6.7	4.3
Government Consumption Expenditure	0.5	5.5	1.9	5.4	-0.2	-1.5	-1.7	0.5	0.5
Total Export of Goods	10.0	14.7	14.2	15.0	18.7	15.3	11.6	15.0	8.9
Domestic Export of Goods	-5.2	-0.2	-7.3	0.8	5.0	-0.6	6.4	2.8	5.2
Re-export of Goods	11.5	16.0	16.3	16.1	19.7	16.6	12.0	16.0	9.2
Import of Goods	8.2	15.7	13.1	16.3	20.3	14.2	7.8	14.4	6.0
Export of Services	10.4	11.8	7.1	12.6	31.4	10.3	8.9	14.5	7.7
Import of Services	-0.3	3.1	-4.6	4.1	30.3	5.8	1.5	9.2	5.7
Gross Investment	0.0	1.9	0.1	5.5	12.7	4.9	3.5	6.5	0.7
Investment in Land & Construction	-6.5	-6.9	-6.7	-6.0	-2.7	-4.6	-3.5	-4.2	-2.3
Investment in Machinery & Equip.	5.6	9.3	6.5	16.0	26.1	12.2	8.5	15.2	3.0
GDP Deflator Growth Rate	-6.0	-4.8	-5.2	-4.1	-2.6	-2.5	-1.7	-2.7	-1.4
CPI (Composite) Inflation Rate	-3.6	-2.3	-2.6	-1.8	-0.9	0.8	0.1	-0.5	0.1
Unemployment Rate	8.3	7.4	7.9	7.2	6.9	6.8	6.7	6.9	6.7
Date of Forecast: January 7th, 2005									

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

	2004									2005		
	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR
Unit Value Trade Index (Domestic Exports)	0.3	0.5	-0.3	0.9	1.6	3.0	3.9	4.4	4.0	3.4	3.0	2.7
Unit Value Trade Index (Imports of Foodstuffs)	3.5	3.6	3.5	4.3	3.5	4.3	4.7	3.9	3.4	3.7	3.5	3.7
Unit Value Trade Index (Imports of Consumer Goods)	-0.1	0.6	1.0	0.8	2.1	2.0	1.9	2.2	1.4	1.9	1.5	2.2
Unit Value Trade Index (Imports of Raw Materials & Semi-Manufactures)	4.7	5.3	5.9	6.7	6.8	7.3	7.6	7.3	6.9	6.7	6.5	5.5
Unit Value Trade Index (Imports of Fuels)	14.2	29.7	30.0	32.3	36.8	42.2	46.8	47.5	52.4	34.0	35.8	35.6
Unit Value Trade Index (Imports of Capital Goods)	-1.4	-1.9	-0.9	0.3	1.1	0.6	0.7	0.7	0.7	1.2	0.2	0.2
Real Retained Imports of Foodstuffs	13.4	17.3	25.3	6.1	3.7	7.7	10.5	-9.3	-4.2	3.1	2.4	-1.3
Real Retained Imports of Consumer Goods	19.8	6.9	37.5	4.6	-13.8	11.2	-17.2	7.5	-4.8	153.0	-55.0	4.4
Real Retained Imports of Raw Materials & Semi-Manufactures	23.3	32.5	-7.4	5.6	10.9	62.8	-9.3	-13.0	-5.6	-4.1	-19.9	-13.8
Real Retained Imports of Fuels	47.9	-2.7	37.4	13.8	11.6	-12.3	9.2	-7.9	-4.1	-6.0	7.3	-16.7
Real Retained Imports of Capital Goods	39.1	10.9	36.7	19.0	25.4	5.3	2.3	-3.6	-5.5	13.8	-19.0	-7.0
Total Motor Vehicles Newly Registered	32.6	36.7	36.1	16.2	17.8	4.2	9.0	18.1	-0.9	14.8	4.3	-9.8
Private Cars Newly Registered	54.9	47.7	40.9	21.4	27.1	11.7	15.8	25.7	5.6	23.1	18.9	-7.3
Volume Index of Retail Sales	20.0	15.7	11.4	8.4	4.0	7.7	7.3	6.8	5.3	0.0	6.5	2.9
Money Supply (M2)	7.6	6.6	6.8	5.9	5.8	6.4	5.7	10.3	10.3	9.2	9.8	15.3
Loans and Advances	-0.1	-0.2	1.1	1.3	2.1	3.0	1.0	6.6	5.8	3.0	1.7	6.3
Visitors Arrivals	19.2	22.4	35.0	40.0	25.6	14.2	18.9	15.8	15.7	9.3	18.2	9.3
Hong Kong Resident Departures	69.9	41.2	19.1	12.4	0.7	8.1	9.4	5.6	3.4	-2.1	11.5	8.4
Electricity Consumption	4.5	-7.1	6.6	2.5	-0.1	2.2	-9.6	15.5	-1.0	4.1	2.4	4.4
Gas Consumption	2.0	0.9	0.8	0.5	-1.3	-0.7	0.2	0.1	-2.1	-1.1	-2.7	-4.2

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