3. Domestic economy

Hong Kong's economy continued to recover moderately in the second half of 2023 amid the robust revival of inbound tourism and consumption demand. Looking ahead, the economy is expected to recover further at a moderate pace, and the growth outlook is subject to increased external uncertainties relating to the US policy rate path, dimmer global economic prospects, the recovery pace of the global tech cycle, and evolving geopolitical tensions. In tandem, various talent attraction and labour importation schemes will continue to help alleviate labour shortages across industries, while local inflation should remain largely in check despite some upward pressures from increasing labour and rental costs.

3.1 Real activities

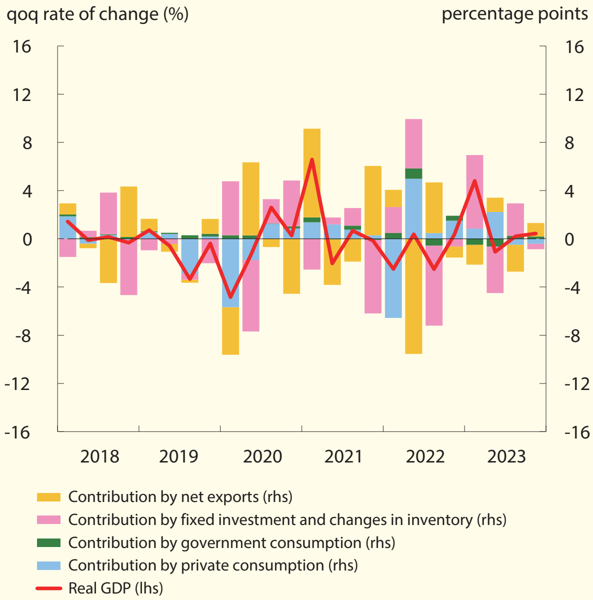
Hong Kong's economy continued its recovery in the second half of 2023, although at a moderated pace compared to the first half. On a year-on-year basis, real GDP grew by 4.1% and 4.3% respectively in the last two quarters of 2023 against a low base of comparison (Table 3.A). For 2023 as a whole, real GDP expanded by 3.2% after a 3.7% contraction in the preceding year.

Table 3.A
Real GDP growth

		Year-on-year growth rate (%)	Seasonally adjusted quarter-on-quarter growth rate (%)
2022	Q1	–4.0	–2.5
	Q2	–1.4	0.4
	Q3	–4.9	–2.5
	Q4	–4.3	0.3
2023	Q1	2.9	4.8
	Q2	1.5	–1.1
	Q3	4.1	0.2
	Q4	4.3	0.4

Source: Census and Statistics Department (C&SD).

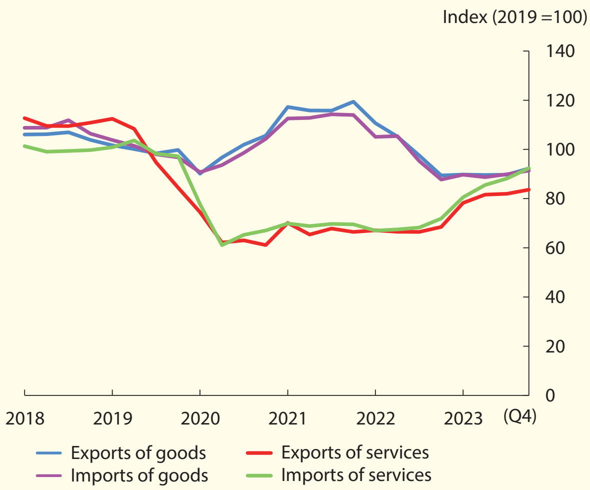
Chart 3.1
Real GDP growth and contribution by major expenditure component



Note: Growth rates are seasonally adjusted.
Sources: C&SD and HKMA staff estimates.

Inbound tourism and consumption demand continued to be the major growth drivers in the second half of 2023 (Chart 3.1). Domestically, private consumption remained robust following a notable expansion in the first two quarters of 2023, thanks to the resilient labour market and the Government's various support measures[23]. Despite the cautious business sentiment amid tightened financial conditions[24], investment spending turned to an increase against a low base of comparison. Externally, Hong Kong's exports of services continued to be resilient on the back of the robust revival of inbound tourism (Chart 3.2). Specifically, total visitor arrivals reached around 34 million in 2023, equivalent to over 60% of the pre-pandemic level in 2019.[25] In contrast, merchandise exports remained sluggish amid weak external demand. Overall, net trade continued to be a drag on real GDP growth in the second half of 2023.

Chart 3.2
Export and import volume



Note: The data are seasonally adjusted.
Source: C&SD.

In 2024, Hong Kong's economy is expected to recover further at a moderate pace, with the Government forecasting real GDP to grow by 2.5% – 3.5% for the entire year.[26] Inbound tourism is expected to be supported by further improvement in Hong Kong's handling capacity and the steady growth of the Mainland China's economy, and local consumption will be underpinned by a resilient labour market. In addition, public infrastructure projects will also render support to the economy. Private investment is likely to stabilise alongside the Government's efforts on attracting businesses into Hong Kong, and merchandise exports may be supported by the expected global tech cycle recovery. That said, the growth outlook is fraught with risks and uncertainties as discussed in previous chapters, especially those relating to the US policy rate path, the prospects for global economic growth, the recovery pace of the global tech cycle, and heightened geopolitical tensions.

23 Including the disbursement of the second instalment of consumption vouchers in July 2023, and a series of promotional campaigns.

24 The Purchasing Managers' Index (PMI) stayed in the contractionary zone (below 50) from July to October 2023, and hovered around 50 between November 2023 and February 2024.

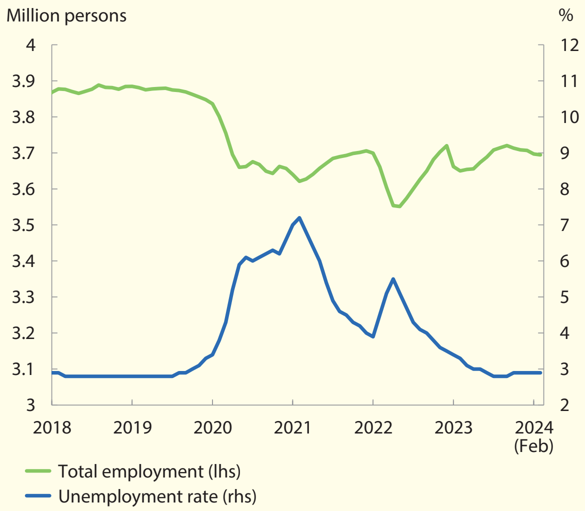
25 On a year-to-date basis (up to end-February 2024), the total number of visitor arrivals amounted to 63.3% of the level in the same period in 2019.

26 The average growth forecasts by private-sector analysts was 2.8%.

3.2 Labour market conditions

The labour market remained resilient in the second half of 2023 and early 2024. The seasonally adjusted unemployment rate stayed low at 2.9% in February 2024, while total employment flattened somewhat and still fell short of its pre-pandemic level (Chart 3.3). Partly reflecting the tight labour market conditions, labour earnings[27] saw an accelerated year-on-year growth of 3.5% in the third quarter of 2023. In response to the manpower shortages across sectors, the Government has introduced various talent attraction initiatives[28] and labour importation schemes. Looking ahead, these measures will help alleviate the manpower shortages across industries[29], while the ongoing economic recovery should continue to support labour demand.

Chart 3.3
Labour market conditions



Source: C&SD.

[27] Measured by the nominal index of payroll per person engaged.

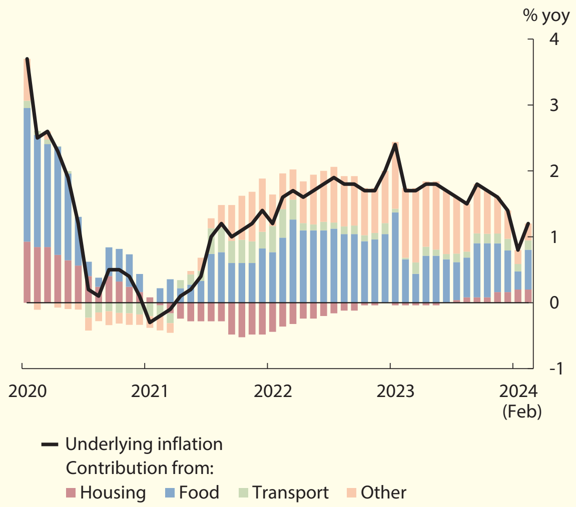
[28] In the 2023 Policy Address, the Chief Executive announced further measures to attract and retain talents, including (i) expanding the list of eligible universities under the Top Talent Pass Scheme (TTPS), (ii) introducing the new Capital Investment Entrant Scheme (CIES), (iii) launching the Vocational Professionals Admission Scheme (VPAS), and (iv) temporarily exempting non-local full-time postgraduate students from the restrictions on taking up part-time jobs in Hong Kong.

[29] Over 220,000 applications under these talent admission schemes were received in 2023, out of which over 130,000 have been approved with about 90,000 talents having arrived in Hong Kong.

3.3 Inflation

Consumer price inflation remained moderate over the past few months. Netting out the effects of all Government's one-off relief measures, the underlying composite consumer price index (CPI) increased mildly by 1.6% in both the third and fourth quarters of 2023, and by 1.2% in February 2024 (Chart 3.4).[30] Analysed by component, inflation momentum of energy-related items decelerated as international fuel prices retreated, while the price of meals out and takeaway food continued to see visible increases. The housing rental component also showed signs of bottoming out amid the feed-through of rising fresh-letting residential rentals (Chart 3.5). Meanwhile, labour cost pressures increased in recent quarters as the labour market remained tight, whereas imported inflation remained steady (Chart 3.6).

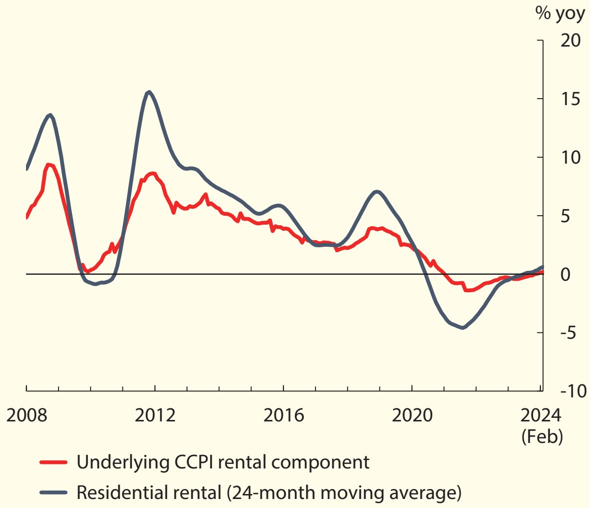
Chart 3.4
Underlying consumer price inflation and its drivers



Sources: C&SD and HKMA staff estimates.

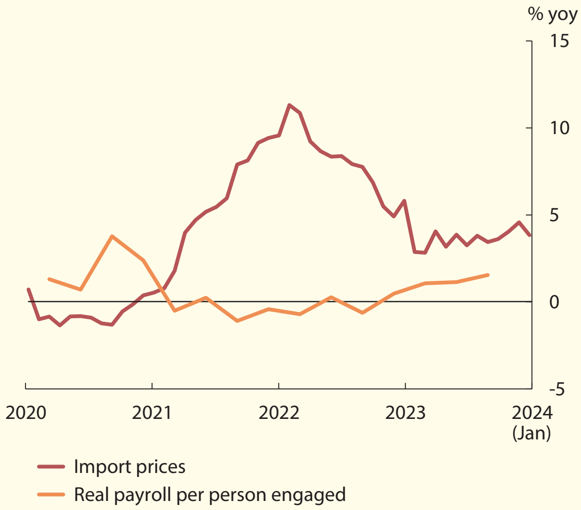
[30] Inclusive of the effects of the Government's relevant one-off relief measures, the year-on-year headline inflation rate was 1.9% and 2.6% in the third and fourth quarters of 2023 respectively, and 2.1% in February 2024.

Chart 3.5
Composite consumer price index rental component and housing rentals



Sources: C&SD and Rating and Valuation Department (R&VD).

Chart 3.6
Labour cost and import prices



Source: C&SD.

In the near term, overall inflation may edge up but remain mild. Domestic business costs may continue to face some upward pressures as the economy further recovers, while rising housing rentals will also gradually pass through to consumer price inflation. In contrast, external price pressures are likely to remain modest. The Government projects the underlying and headline inflation rate to be 1.7% and 2.4% respectively in 2024.[31]

31 The market consensus forecasts of the headline inflation rate for 2024 was 2.2%.