

Employment Growth: Analyzing the Internal and External Factors

After a brief contraction in Q2 2003, Hong Kong's economy has resumed its growth momentum. More encouragingly, improving economic conditions have pulled the sluggish job market out of its slump. The unemployment rate has dropped from 8.7% in July 2003 to 6.9% in June this year. In the past, both internal and external forces worked together to drive employment growth. Yet this time, external factors have supplied much of the fuel to power the job market's upturn.

Identifying the sources of employment growth

Between Q3 2003 and Q1 2004, external forces directed the job creation process. Specifically, the import/export trades, wholesale/retail and restaurants/hotels all recorded strong employment growth. Employment in real estate and business services rose modestly. On the other hand, employment failed to pick up in construction, as well as public administration, education, medical, and other health and welfare services.

Employment Growth between 2003Q3 and 2004Q1	
<i>Industries</i>	<i>Change in Employed Persons (persons)</i>
Import/Export Trades	54,900
Wholesale/Retail, Restaurants/Hotels	20,000
Real Estate and Business Services	8,600
Construction	-5,100
Public Administration, Education, Medical, and Other Health and Welfare Services	-4,700
Others	-11,500
Total	62,100

Source: Quarterly Report on General Household Survey

Surging exports

The trade sector has been an important job creator in the current recovery. The sector has always been a major contributor to the job market, even before its recent stellar performance. Yet from 2002 to the first half of 2003, employment growth stagnated despite strong export growth.



There are two possible explanations for this phenomenon. Part of the increase in trade activities in the past few years was driven by foreign companies relocating their manufacturing processes to China. As a result, an increasing share of trade involved the transportation of semi-finished products, such as computer motherboards and electronic components, from parent companies overseas to Mainland assembly lines. Significantly fewer economic activities took place in Hong Kong, compared to the traditional trade in re-exports. Furthermore, trading companies were still recovering from the aftermath of the Asian Financial Crisis, with many saddled with negative equity. The uncertain global economic outlook and the SARS outbreak compromised their willingness to expand their workforce. As a result of all these factors, the pickup in trade activities failed to stimulate employment.

Compared to the situation in 2002, the latest increase in exports has boosted employment significantly, as traditional trading activities have surged following the recent recovery in the re-export trade to the US and other regions. Moreover, rising property prices have improved trading companies' financial position, and the recovery in the global economy has reaffirmed the pickup in trade activities. Total exports jumped by 15.5% in the first half over the same period last year. As the worrying factors are gradually turning into distant memories, the trade sector is expected to become a major driving force in Hong Kong's job market once again.

Vibrant tourism

Another bright spot is the rise in employment in domestic consumption market, in which surging tourist arrivals have played an important role. The introduction of the Individual Visiting Scheme (IVS) at the end of July 2003 has spurred mainland tourist arrivals. In addition, tourists from other countries have started to return after the end of the SARS outbreak. In the first quarter this year, total consumption expenditure in the domestic market grew by \$7.5 billion compared to the same period last year, and tourist spending accounted for 36% of the increase. Since tourists spent a large portion of their travel budgets on shopping, meals, and hotels, these industries have benefited the most from the surge in tourist arrivals. From 3Q 2003 to 1Q 2004, 20,000 new jobs were created in these sectors.

Vibrant tourism will continue to provide a strong lift to employment this year. The recent expansion of IVS to nine more cities outside Guangdong effectively bolsters the number of eligible mainland visitors to 150 million. Non-mainland tourists are expected to increase as the global economy continues its steady growth. We estimate that total tourist arrivals will grow by 38% to 21 million this year, and will help generate 11,400 jobs in the retail, restaurant, and hotel industries in 2004.

The pace of visitor arrivals will slow down next year when the SARS-induced low-base effect disappears. Nevertheless, the scheduled opening of the Disney Theme Park in 2006 will turn Hong Kong into a major tourist site once again. Overall, we expect tourism to create 7,500 jobs in 2005 and 11,500 in 2006 in the retail, restaurant, and hotel industries.

Rising demand for business services

The real estate and business services sector was another strong performer during the recent revival in the job market. Similar to the trade sector, the business services industry has always been a steady job creator under the benefit of the growing China market. Between 1998 and 2000, employment in real estate and business services continued to grow despite the sluggish local property market. However, growth has stagnated since then. Advances in the mainland's infrastructure and cost-cutting practices within the sector triggered the relocation of back-end jobs, such as data processing and call centers, to the north. Employment growth within the sector languished as a result.

However, employment in real estate and business services returned to a rising trend between Q3 2003 and Q1 2004, adding 8,600 jobs. While the upturn was reinforced by the revival in the local property market, it was also affected by the end of the current cycle of corporate restructuring. China's gradual march to a service-based economy will generate huge demand for business services, and the superior experience and expertise of Hong Kong-based professionals will ensure them a share of this lucrative market. This will continue to benefit employment growth in the sector.

Shortage of construction projects

While external factors provided a much-needed boost to overall employment, the internal sector has lagged behind in the job creation process. The 1997 Asian Financial Crisis and the subsequent crash in property prices weakened the outlook for the property market, forcing developers to reduce the number of construction projects on both the commercial and residential fronts. As a result, the total number of completed office, commercial, and factory space fell from 975,000 sq.m in 1998 to an estimated 377,000 sq.m. in 2004, while the number of completed private and public housing units decreased from 49,000 to an estimated 26,400 during the same period.

The construction industry lost 5,100 jobs between Q3 2003 and Q1 2004 and has been downsizing since 1997. Worse still, the sector has little chance to reverse its fortunes in the near future. The lack of construction projects has forced developers to trim their workforce. The latest forecast issued by the Housing, Planning and Lands Bureau indicates that new supply of private residential units will drop over the next four years to an estimated 16,200 in 2007 and 11,400 in 2008. Furthermore, KCRC will not invite expression of interests for their residential development projects before 2005, and MTRCL will not provide new residential flats in the coming three years except those already under construction, thus extending the hiring drought.

Persistent budget deficit

The sluggish process of job creation in the internal sector is heightened by the reduced hiring in the public sector. During the difficult years immediately following the Asian Financial Crisis, public sector hiring gave much support to the labor market. Yet, between Q3 2003 and Q1 2004, the year-on-year growth of employment in public administration as well as education, medical, and other health and welfare services has turned negative.

Unlike the private sector, which looks set to benefit from better economic conditions, the public sector will continue to be constrained by the government's tight financial position. Finance Secretary Henry Tang stated in The 2004-05 Budget that the government will experience a fiscal budget deficit of HKD 49 billion in F2004/05, equivalent to 4% of GDP, and the fiscal balance sheet is not expected to return to the black before F2008/09. To restore fiscal balance, the government declared that it will cut the establishment to 160,000 by F2006/07. This leaves the public sector little room to create new jobs in the near future.

Conclusion

The recent revival in employment has been largely driven by vibrant tourism, rising trade activities, and strong demand for business services. Private consumption is expected to pick up on the back of gradually improving consumer confidence. This, together with strong tourism growth, will help sustain employment growth in the retail and restaurant industries. The improving global economic environment will provide further stimulus to Hong Kong's trade sector and business services industry. The trade sector is likely to be shielded from the negative effects of Beijing's macro measures to cool the Chinese economy, as most of the goods exported from Hong Kong to China are for outward processing. The pace of improvement in the unemployment rate situation will be moderated by the weariness of the construction industry and downsizing in the public sector. Nevertheless, the positive will outweigh the negative, and unemployment rate is expected to fall to 6-6.5% by year-end, and could reach 5.5% by 2005. Real GDP is projected to grow by 7.0% in 2004.