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Hong Kong Food Inflation

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Report Highlights:

Food inflation in Hong Kong reached 7 percent in 2011, while Hong Kong's year-on-year overall consumer price index (CPI) for 2011 rose 5.3 percent after reaching a high of 7.9 percent in July 2011. Food (27.45% of CPI basket) is the second largest expenditure item following housing (31.66%) in Hong Kong, meaning food price increases have a significant impact on the overall inflation rate. In addition, Hong Kong's relies heavily on food imports from China. Thus, China's food prices are a key factor affecting Hong Kong's inflation rate. With the slowdown in local economic growth and the gradual decline in food inflation in China, the Hong Kong government forecasts that the average inflation rate for 2012 will drop from 5.3 percent in 2011 to 4 percent this year.

Overall Inflation in Hong Kong

Hong Kong's 2011 inflation rate reached 5.3 percent, which was even higher than the 4.3 percent in 2008 when there was worldwide inflation caused by rising global food prices. Inflation in 2011 resulted from a bundle of factors including rising food prices in China and depreciation of Hong Kong dollar against Renminbi.

Hong Kong's inflation peaked in July 2011 at a rate of 7.9 percent. With the slowdown in local economic growth and the gradual decline in food inflation in China, the rising trend in Hong Kong's inflation statistics started to taper in the fourth quarter of 2011. While Hong Kong's economy registered notable growth of 5% in 2011 after expanding by 7% in 2010, the economy is forecast to grow at 1-3% for 2012. As a result of the expected economic slowdown coupled with global food and commodity prices retreating from peaks, the Hong Kong government forecasts that the inflation rate will drop to 3.5 percent this year.

The Role of Food in Overall Inflation

Housing and food carry the two largest expenditure weights in the context of Hong Kong's consumer price index, with weights of 31.66 and 27.45 percent respectively, while all other items merely account for a single digit share except for the miscellaneous items category (15.87%). (Miscellaneous includes expenses on education, package tour, medical services, etc.) Thus, housing and food have a determining role for Hong Kong's inflation rate. The figure below depicts the trend of Hong Kong's overall inflation rate compared to that for food. It is discernible that they are of similar trend signifying the role of food prices in Hong Kong's inflation rate.

Figure 1: Hong Kong: Price Trend for all Items compared to Food



Source: Hong Kong Census & Statistics Department

Among various expenditure items, food and housing experienced some of the highest increase rate changes in 2011 with rates of 7 and 7.2 percent respectively. Prices for tobacco surged exceptionally high (17.1%) due to an increase in the tobacco duty.

Table 1: Hong Kong: Consumer Price Index (%)

	Weight %	2010	2011	2012 Jan	2012 Feb
All items	100	2.4	5.3	6.1	4.7
Food	27.45	2.4	7.0	8.2	6.7
Meals away from home	(17.07)	1.7	5.2	6.5	6.0
Food, excluding meals away from home	(10.38)	3.5	9.9	10.9	7.9
Housing	31.66	0.4	7.2	8.5	8.1
Electricity, gas and water	3.10	43.3	-4.2	-15.6	-17.4
Alcoholic drinks and tobacco	0.59	3.4	17.1	19.5	16
Clothing and footwear	3.45	1.8	6.8	5.4	5.4
Durable goods	5.27	-2.7	-3.8	-2.4	-1.8
Misc. goods	4.17	2.4	3.8	3.0	3.8
Transport	8.44	2.0	4.4	4.6	4.2
Misc. services	15.87	2.0	3.5	5.6	0.5

Source: Hong Kong Census & Statistics Department

Hong Kong food inflation is closely related to food prices in China as many major staple food supplies (such as vegetables, meats and eggs) are often supplied by Mainland China. In 2011, Hong Kong imported over 17 percent of its agricultural and food products from China, followed by the U.S. (16%) and Brazil (8%).

Given the close food supply correlation between Hong Kong and China, it is not surprising that the inflation rate of Hong Kong follows that of China. China's inflation hit 5.4 percent last year with food items as the key driving force because it accounts for about one-third of the weighting in its Consumer Price Index (CPI) calculation. Mainland food prices last year soared 11.8 percent. However, after escalating to a high of 6.5 percent in July, overall inflation has gradually fallen since then.

Table 2. Hong Kong: Imports of Agricultural and Food Products by Major Suppliers

Hong Kong Import Statistics							
Commodity: Agricultural, Fish & Forestry, Group 1 (2007)							
Year To Date: January - December							
Partner Country	United States Dollars			% Share			% Change
	2009	2010	2011	2009	2010	2011	2011/2010
World	15,828	19,074	22,447	100.00	100.00	100.00	17.68
China	2,933	3,280	3,881	18.53	17.20	17.29	18.32
U.S.	2,269	3,151	3,685	14.33	16.52	16.41	16.93
Brazil	1,661	1,491	1,746	10.49	7.82	7.78	17.13
Japan	794	1,075	1,078	5.02	5.64	4.80	0.31
France	456	696	1,006	2.88	3.65	4.48	44.49
Thailand	869	804	879	5.49	4.22	3.91	9.27
Australia	743	745	868	4.69	3.90	3.87	16.51

Source: Hong Kong Census and Statistics Department

Given the limited size of living spaces and modest home kitchens, Hong Kong consumers have a habit of eating out, particularly for lunch and weekends. Eating out accounts for 17.07 percent of overall expenditure, whereas food excluding meals bought away from home only accounts for 10.38 percent. Alternatively, it can be said that 62 percent of Hong Kong consumers' expenditure on food is spent by eating out, whereas the remaining 38 percent is spent for food consumed at home. Big expenditure items include fresh vegetables (1.16%), pork (1.15%), bread and biscuits (0.79), marine fish (0.75%) and fresh fruit (0.71%).

Food Inflation

While Hong Kong's food prices surged 7 percent in 2011, the rate has slackened in early 2012 with the first two months together rising only 5.4 percent compared to the same period last year. The food index for February 2012 rose 6.7 percent, smaller than the corresponding increase (8.2%) in January 2012. The smaller increase, particularly in February, was achieved in part due to the timing of the Chinese New Year in January this year compared to February last year. (The Chinese New Year is always associated with increased food prices particularly for expensive food items and eating out.)

February 2012 to February 2011 figures were compared. The food items that experienced the greatest price increase included marine fish (20%); fresh water fish (17%); beef (16%), meats - other than beef,

pork and poultry (15%); processed seafood (15%); pork (14%); canned meats (13%); and eggs (12%). These food items share one common feature – China is a major supplier. (Note: Beef and pork refer to freshly slaughtered products.) Marine fish accounted for the most conspicuous price increase as a result of rising demand for expensive seafood items in China. As keen demand in China can support high prices, there is less incentive to supply these products to Hong Kong. Thus, prices in Hong Kong rise.

Table 3. Hong Kong: Food Price Index

	Weight %	Price Index Growth %	
		Feb 12/11	2011/2010
All items	100	4.7	5.3
Food	27.45	6.7	7
Meals bought away from home	17.07	6.0	5.2
Food, excluding meals bought away from home	10.38	7.9	9.9
Rice	0.33	2.0	0.9
Other cereals and cereal preparations	0.26	6.8	4.5
Bread, cakes, biscuits and puddings	0.79	5.5	6.5
Salt-water fish	0.75	20.2	20.5
Fresh-water fish	0.41	17.2	14.1
Other fresh sea products	0.29	11.2	23
Processed sea products	0.48	14.6	14.9
Pork	1.15	14.3	18.5
Beef	0.22	15.5	11.4
Poultry	0.40	4.3	8.7
Meat, frozen	0.42	9.3	7.6
Meat, canned	0.07	13.3	6.1
Meats, others	0.42	14.7	12.7
Fresh vegetables	1.16	0.7	1.7
Processed vegetables	0.05	5.9	6.2
Fresh fruit	0.71	0.6	10.9
Processed fruit	0.03	7.6	14.4
Dairy products	0.47	7.2	6.5
Eggs	0.13	12	7.8
Edible oils	0.16	6.6	7.7
Carbonated drinks	0.08	7.6	1.9
Other non-alcoholic beverages	0.31	4.8	4.5
Sugar	0.02	8.5	8.8
Confectionery	0.15	9.1	8.2
Flavorings and additives	0.13	5.3	5.0
Food, others	0.99	3.1	5.5

Source : Hong Kong Census & Statistics Department

Correlation between Hong Kong and China's Food Prices

China's CPI for food had a remarkable rise of 11.8 percent in 2011. Food prices helped drive inflation

as they account for about one-third of the weighting in its CPI calculation. The overall inflation rate in 2011 was 5.4 percent. After hitting a high of 6.5 percent in July 2011, inflation has gradually fallen since then. China’s inflation for all items and food in March 2012 were recorded as 3.6 and 8 percent respectively. The government’s inflation target for the year is 4 percent.

The table below shows the year-on-year inflation rate of Hong Kong compared to that of China. The trend of the two economies is very similar; both experienced a peak in July and have seen a declining rate trend since then.

Figure 2. Price Trend between Hong Kong and China



Source: Hong Kong Census & Statistics Department
National Bureau of Statistics of China

As China is Hong Kong’s largest food supplier, the inflationary food price changes in China have been transmitted to Hong Kong and will continue to impact Hong Kong accordingly. China supplied about 93 and 100 percent of live pigs and cattle slaughtered in Hong Kong. Thus when the price for fresh pork in China increased drastically by 37 percent in 2011, it is not surprising that pork prices in Hong Kong also soared by 18.5 percent. Similarly, China’s prices for poultry eggs last year rose by 12.6 percent, fuelling a corresponding price index increase in Hong Kong by 7.8 percent. Given the rising prices in China, Hong Kong market share for eggs supplied from China dropped from 59 percent in 2010 to 55 percent in 2011. It is worth noting that when the price index for vegetables recorded a moderate growth of 1.7 percent in China, the corresponding price index in Hong Kong also showed only moderate growth of 3.4 percent.

Table 4. Hong Kong: Correlation between Hong Kong and China food Prices

	Year-on-Year 2011 Price Index in Hong Kong (%)	Year-on-Year 2011 Price Index in China (%)	Year-on-Year 2011 Produce Prices in China (%)

All items	5.3	5.4	-
Food	7	11.8	
Pork, fresh	18.5	-	37
Beef, fresh	11.4		8.1
Vegetables	3.4	-	1.7
Poultry eggs	7.8	-	12.6
		-	

Source: Hong Kong Census & Statistics Department
National Bureau of Statistics of China

Additional Factors

Apart from rising food prices in China, there are other factors playing a role for Hong Kong's food inflation. The exchange rate of the Hong Kong dollar against Chinese Renminbi has certainly posed upward pressure on Hong Kong food prices. The Renminbi appreciated by 5 percent against Hong Kong dollar last year (January 4, 2011 One Hong Kong dollar = 0.851 Chinese Yuan; December 30, 2011 One Hong Kong dollar = 0.812 Chinese Yuan.) Hong Kong dollar's depreciation has been translated into rising costs ultimately affecting the rate of inflation. As noted previously, many staple supplies such as fresh vegetables, fresh pork and beef are not easily replaceable with supplies from other places given the advantage of geographical proximity between Hong Kong and China. Neither are they necessarily fully substitutable because of consumption habits often favor the characteristics of the Mainland product.

A strong economy in 2011 and the implementation of minimum wage all fuelled the high inflation rate with varying degree of impact. Hong Kong's economy registered a notable growth of 5% in 2011, after expanding by 7% in 2010. The economy sustained strong momentum on entering 2011 though growth moderated since the second quarter amid a slowdown in global demand. Hong Kong's first ever implementation of minimum wage has also been used as a justification for the food industry, particularly the fast food catering outlets, to raise prices.

Moreover, supermarket chains tend to maintain (or deepen) their profit margin by raising selling prices when costs increase. Given the dominating market share of these retail outlets, the impact on overall inflation is large. The Hong Kong Consumer Council conducted a survey showing the inflation rate of a basket of 200 items sold in three dominating supermarket chain stores. Comparing the survey with the government statistics for the inflation rate of specific food items, it was found that food sold in supermarkets had price increases far more significant than those obtained elsewhere. (The government sourced samples all over Hong Kong from a variety of outlets not just limited to supermarkets.) For example, egg prices in supermarkets last year rose 14.2 percent which was in stark contrast to the 7.8 percent rate recorded by government statistics. Prices rose 11.9 percent for canned meat products sold in supermarkets compared to 6.1 percent for those sold in other places.

Food Inflation based on Hong Kong Consumer Council's Survey

Based on a 2011 supermarket price survey conducted by the Consumer Council, the average price of a basket of 200 items of food and household products rose 5.1 percent. The 200 items were grouped

into 12 categories or 42 sub-categories. The aggregate average price of the 12 main categories had their prices increased ranging from 1.5 percent to 11.7 percent in 2011. Among them, canned food/prepackaged soup (11.7%), pre-packed bread/cakes (9.9%) and dairy products/eggs (8.2%) topped the list.

While the result is in line with the government overall inflation rate of 5.3 percent, the supermarket price analysis did not take into account some key inflation factors such as housing, eating out expenses, and transport. The survey also excluded fresh meats and fruits which contributed significantly within the food inflation category.

Comparing the Consumer Council survey, which is based on three dominant supermarket chains in Hong Kong to the government food inflation statistics, the price increase rate in supermarkets far exceeds the government figures for a wide variety of food items ranging from eggs, canned meats, bread and cakes to carbonated drinks, with the only exception being confectionery items. A side by side inflation rate comparison is provided in the chart and table below.

Figure 3. Rate of Price Change between Consumer Council Survey and Government Statistics

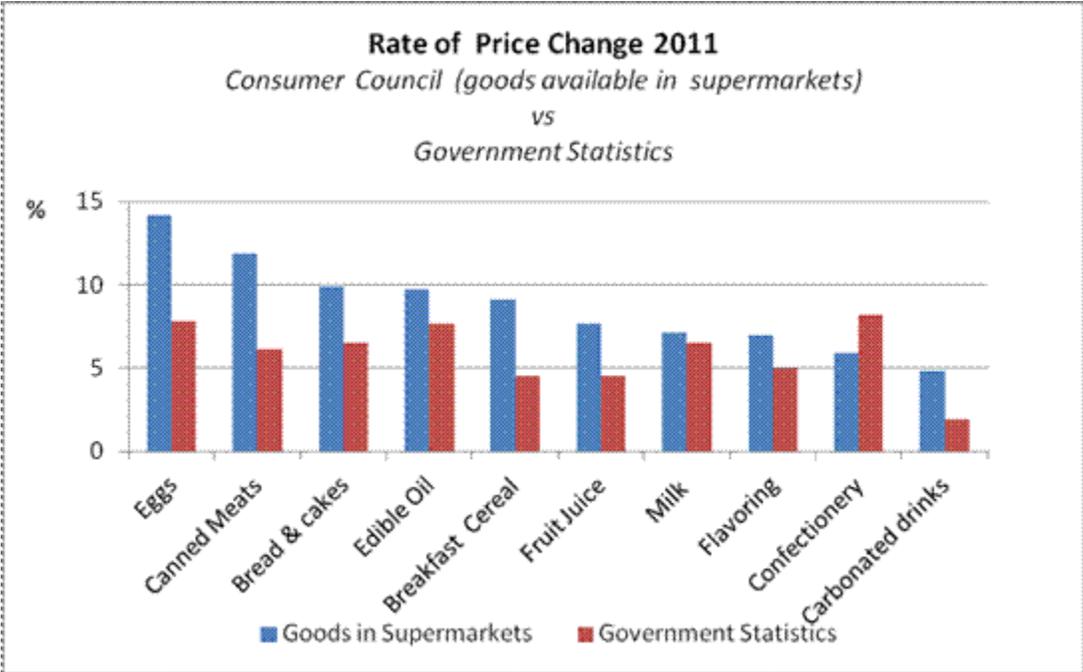


Table 5. Comparison of the Inflation Rate between Consumer Council Survey and Government Statistics

Consumer Council Survey (goods available in supermarkets)	Government Statistics
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Product Categories	Inflation Rate %	Product Categories	Inflation Rate %
Canned fish	15		
Butter	15		
Eggs	14.2	Eggs	7.8
Prepackaged cake	13.4	Bread, cakes, biscuits and puddings	6.5
Milk Powder	12.3		
Canned Meats	11.9	Meat, canned	6.1
Edible Oil	9.7	Edible oils	7.7
Breakfast Cereal	9.1	Other cereals and cereal preparations	4.5
Noodles	8.2		
Instant Coffee	8.1		
Fruit Juice	7.7	Other non-alcoholic beverages	4.5
Canned soup/vegetables	7.3	Processed vegetables	6.2
		Processed fruit	14.4
Nuts	7.2		
Milk	7.1	Dairy products	6.5
Flavoring	7	Flavorings and additives	5
Ice Cream	6.7		
Bread	6.5		
Soya milk	6.3		
Instand noodles	6.3		
Chocolate/confectionery	5.9	Confectionery	8.2
Beer	5		
Frozen food	4.8		
Carbonated drinks	4.8	Carbonated drinks	1.9
Chips	4.1		

Source : Hong Kong Consumer Council 2011 Supermarket Price Survey
Hong Kong Census and Statistics Department