



Hong Kong's Role in China's Future Economic Development

Tse Kwok Leung, Head of Economic Research Division

Four decades of China's reform and opening up has created an economic growth miracle. Hong Kong has seized the opportunity to become the major participator in introducing capital and technology as well as expanding the international market for the Mainland China, with Hong Kong's companies acting as pioneers in many aspects in the early stage of foreign investment entering the Mainland. On November 12, President Xi Jinping summed up the six major roles played by Hong Kong in the country's reform and opening up in a speech to a Hong Kong and Macao delegation to celebrate the 40th anniversary of the country's reform and opening up in Beijing. These roles include: the leading role in investment and in industry prosperity, the demonstration of market economy, the booster for institutional reform, the bridge of two-way opening-up, the pilot place for a first try, the reference of urban management. President Xi's evaluation has fully affirmed the special status, unique role and major contribution of Hong Kong and Macau in country's reform and opening up.

Looking back on the course of forty years, Hong Kong's functional role in the country's economic development and take-off process is not static, but has undergone several adjustments and transformations, showing strong flexibility and adaptability. Hong Kong has transitioned from a trade intermediary in the early stage to the introducer of capital and technology, then to the center of financing and producer service, and further to become an important base for Chinese enterprises to list and to operate. In recent years, Hong Kong has provided asset management services for the Mainland, has served as the platform for Chinese companies going abroad as well as the offshore market for RMB internationalization, and has proactively participated in the Belt and Road Initiative (BRI) and the construction of the Greater Bay Area. Through the cooperation with the Mainland, Hong Kong has made positive contribution to the Mainland's structural reform and economic development in the past forty years. At the same time, Hong Kong has benefited from the nation's development by greatly expanding its scope of financial services, and has gradually transformed into a global service economy, with the share of the services sector in GDP printing 93%, being the world's third largest financial center and top Asian location for multinational corporations to set up regional headquarters.

“Leveraging Hong Kong's Advantages and Meeting the Country's Needs” becomes the new foundation for Hong Kong to serve the Mainland

As the Mainland has become the world's second largest economy and the world's biggest trading nation, whether Hong Kong can continue to play a unique role in the country's future reform and opening up is an important topic to discuss. At a meeting with top officials and business leaders from Hong Kong and Macau, President Xi Jinping has indicated that Hong Kong and Macau will continue to play unique and irreplaceable role in China's future development and expressed his four hopes for these two special administrative regions, including more proactively contributing to the country's new round of high-level opening-up,

integrating into the country's overall development, participating in national governance, and being more proactive in promoting international humanities exchanges. These four hopes provide macro guidance to Hong Kong and Macau's new contribution to the country in the New Era. To seize the opportunity and make more achievement, Hong Kong should well respond the complex and changeable global environment, carefully study the national conditions, well understand the new round of reform and opening up direction, policy opportunities and required services, and discover its own strengths and weakness to eventually reposition itself in the country's future economic development.

In terms of meeting the country's needs, as the Mainland developed rapidly and aligned with the international market gradually, traditional functions and strengths of Hong Kong in serving the Mainland's economy has diminished. For example, the proportion of Hong Kong's re-exports of Mainland origin to the Mainland's total export has dropped from the peak of more than 70% to just 10.6% in 2017. In terms of the actually utilized FDI, the share of actual investments from Hong Kong to the Mainland's actual amount of foreign capital has decreased from the peak of more than 70% to 53% in 2017.

In the future, the Mainland, especially the relatively developed regions such as the Pearl River Delta and the Yangtze River Delta, has entered the key phase of upgrading and transformation towards the medium developed economy. The major bottlenecks it encounter are no longer the capital, technology and market in the early stage, but the promotion of modernized, standardized and international management and services in the innovative, coordinated, green, open and shared development. For example, the suitable mechanism for poverty reduction and coordinated regional development ; the modernized management for the urbanization ; the standardized systems and rules for improving the level of marketization in coastal economically developed regions ; the financing facilities and market environment required for the development of private enterprises and small and medium-sized enterprises; the services related to cross-border financing, risk management and legal assistance for the large Chinese enterprise going abroad; the first-hand pilot offshore market for accelerating the renminbi as a major international currency; the talents and intellectual property protection for the core technology research and development in the innovation and technology

In terms of Hong Kong's advantages, "one country, two systems" principle has functioned well. The Central Government firmly supports the Chief Executive and the SAR Government in governing Hong Kong in accordance with the Basic Law. Hong Kong's economy remains prosperous and stable, and its international financial, trade and shipping centres are firmly established. Hong Kong maintains the status of the world's freest economy, and its international competitiveness and business environment are among the highest in the world.

Hong Kong still has several unique strengths in serving the country's development. First, favorable location. Hong Kong is adjacent to the Mainland and has established very close economic and trade ties with the Mainland. Hong Kong is located in the heart of Asia, the population and GDP covered by the four-hour flight is the highest in Asia. The time zone and financial markets are connected with New York and London, playing the role complimentarily with New York and London as the financial and business hub for economic globalization. Second, an independent and sound legal system. Aligned with common law system, Hong Kong has natural advantage to become the connecter between the Mainland and the international market system. Third, developed financial market and financing capability. Four, a clean and efficient government. Five, simple and low tax system. Six, business facilitation. Hong Kong is ranked fourth globally on the ease

of doing business according to the World Bank's Doing Business 2019 Report.

Reinforce advantages and provide high standard services to the country's economic development in the new era

In order to continue to play an important role in the future development of the country's economy, Hong Kong must maintain the predecessors' spirit of the "pioneers" who were dare to be first; must accurately look at and actively cooperate with the needs of the country in the new era of reform, opening up, and innovation, and give full play to its own advantages and strengths to provide higher standards of service for the country's future economic development.

1) Served as an international operation platform for Chinese enterprises. Hong Kong is currently largest and most concentrated offshore operation base in the world for Chinese enterprises, and is the extension of the Mainland onshore market to the international market. During the past several years of providing the investment and financing services for Chinese enterprises, Hong Kong has accumulated abundant experience and a variety of talents, such as fund managers and security analysts. Adding the favorable location, low taxation and satisfied services, Hong Kong has become the best offshore base of financing and operation for Chinese enterprises going abroad.

2) Functioned as separate customs territory and legal service. Hong Kong has been a separate customs area all the time and is the membership of GATT and WTO. On December 19th 1984, the Sino-British Joint Declaration and its annex authorized Hong Kong to continue to maintain its free port and separate customs territory after 1997, to decide its foreign economic and trade policy and to participate in the World Trade Organization using the name of "Hong Kong, China,".

According to The Rules of Origin Agreement of the WTO, Hong Kong, as a separate customs territory which is closely linked with the international market, is well positioned to attract Chinese enterprises to develop high-value-added industries, and to serve as an intermediary platform for technology exchange and transaction worldwide. At the same time, Hong Kong can act as mediation and arbitration center in the resolution of disputes and frictions arising from overseas investment of Chinese enterprises, providing legal assistance for Chinese enterprises going abroad.

3) Act as the frontier of RMB internationalization. To serve as an international currency, RMB has to fulfill the three functions including means of payments, unit of account and store of value. Building up these functions requires the promotion of cross-border transactions and the full-convertibility of capital account, ultimately realizing the full convertibility of the RMB under the capital account. As the largest offshore hub in RMB trade settlement, Hong Kong can help promote the international use of RMB supported by material goods transactions, enhancing the function of RMB as an international currency for transaction and payment. At present, HKD as an international use currency and the free convertibility of RMB in Hong Kong offshore market could provide facilities of currency exchange, payment and transaction to overseas investment of Chinese enterprises.

4) Play a unique role in innovation and technology development of the Guangdong-Hong Kong-Macao Greater Bay Area. Technology and innovation is the first driving force to lead the construction of

the Greater Bay Area, also the most important area for the cooperation between Guangdong, Hong Kong and Macau in the construction of the Greater Bay Area. Chinese vice-premier Han Zheng instructed the leading group of the Greater Bay Area Construction in the first plenary meeting to build a Guangzhou-Shenzhen-Hong Kong -Macau Technology and Innovation Corridor and build the the Bay Area International Technology Innovation Center.

Hong Kong has several advantages and can play an important role in the development of innovation technology and the creation of a high-tech industrial chain in the Greater Bay Area. These including: (1) The state supports Hong Kong to be an international technology and innovation hub. There are many opportunities and space for cooperation between Hong Kong and the Mainland in creative technology; (2) Hong Kong has sound legal system, strong protection of intellectual property rights, and simple and low taxation; (3) With a regulatory amendment Hong Kong now can provide diversified and international financing channels for the new-economy enterprises; (4) By leveraging the role of free port and independent customs zone, Hong Kong can explore the oversea markets for selling high-tech products of the Greater Bay Area.

5) Play a demonstration role in the construction of the business environment and rules for the Mainland. President Xi Jinping said in the Keynote speech of 1st China International Import Expo that China must accelerate the construction of a world-class business environment. Another new role of Hong Kong is to target the Mainland's ongoing reform in the market economy system and administrative management system, and summarize some effective experiences in the standardized operation of the market economy for the Mainland's reference. Experiencing the break-in and collision of Chinese and Western cultures, Hong Kong has developed from a small fishing port into an international financial center that integrates Chinese and Western culture and civilization, and a relatively mature rule of law society. Therefore, in the process of improving the market economy operation mechanism and creating a first-class business environment in the Mainland, Hong Kong can provide some valuable lessons: such as the spirit of contract; transparent business and industry operations; more open and transparent decision-making procedures and governance; more developed social professional management.

Looking ahead, facing rapid development of the country, Hong Kong needs to reinforce its advantages in the rule of law and internationalization, strengthening itself from: (1) Consolidate the close ties of Nylonkong in capital, information and technology, and enhance the ability to lead regional financial innovation and crisis management; (2) Actively cooperate with the Mainland to deepen the institutional arrangements for market interconnection, and deepen the economic and financial cooperation among Guangdong, Hong Kong and Macau; (3) Actively respond to the development trend of international financial supervision after the global financial crisis in 2008, review the current financial regulatory framework, and consolidate and enhance the ability of the financial system to serve the development of emerging markets; (4) Actively capture the need of the state to improve the right to speak in the financial affairs and the international status of the renminbi, making the offshore RMB market bigger and stronger. As long as daring to innovate, and taking advantage of the situation, it is believed that Hong Kong's unique role in the country's reform and opening up in the new era will be strengthened rather than weakened.