Hong Kong: This Century and the Next

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In Hong Kong, as one might expect, we pay close attention to what China says and does. We watch closely because it is now fewer than a thousand days until Hong Kong and China begin their bold experiment in reunification. On the last day in June of 1997, the British flag will come down for the last time, and before sunrise the next morning, sovereignty over Hong Kong will transfer from Britain to China.

The reality is that Hong Kong has emerged as the major service and distribution center for much of Southeast Asia. It is the city in Asia where more companies maintain their regional headquarters than any other. It is a regional and global financial center, and home to the seventh-largest stock market in the world. It is also the widest doorway to China's huge and fast-growing economy, as well as a primary conduit for the rising tide of goods and commodities flowing from China. Hong Kong is, in short, a key jumping-off place for the rest of Asia.

However, more than its economic transformation, it is Hong Kong's social and political status that has begun to fascinate observers around the globe. Despite being the eighth-largest export economy in the world, many see Hong Kong as a pawn in Sino-British relations. As a colony whose sovereignty will pass to China in 1997, Hong Kong is viewed as merely a small piece in a larger game of power politics. Others look on Hong Kong as a "litmus test" of China's transformation or progress toward their own vision of a more liberal, market-oriented

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society and if China can successfully manage Hong Kong's capitalist system after 1997, it will presumably pass.

However, those are very narrow views of Hong Kong. A British observer, William Rees-Mogg, sees it in a broader and more appropriate context: "In terms of understanding the twenty-first century, Hong Kong is a university, Los Angeles a high school, London a primary school and Brussels an old-fashioned kindergarten." When he talks of Hong Kong as a university, what he really means is that it is a city built on the old-fashioned virtues of education, self-discipline, honesty and hard work. It is a place where people believe in risk and reward, capitalism, and the freedom to succeed.

The role of Hong Kong and its future in Asia can be assessed through an examination of its past, present, and future economic development; its role as South East Asia's leading city for regional services, shopping, and finance; and its transition to Chinese rule.

Hong Kong Today

Hong Kong is one of the most vibrant, modern, and prosperous cities in the world, whose own wealthy consumer market has a per capita buying power greater than that of Great Britain. It is the primary tourist attraction in Asia, which helps to explain why Hong Kong not only has a large and profitable hotel industry of its own, but also why its companies now manage several of the largest and most lucrative international hotel chains in the world.

One indication of Hong Kong's emergence as an international center is the growing number of expatriates who live and work there. Nearly as many Canadians live in the territory as British, for example, and there are more Americans than either of them. There are even 120,000 in Hong Kong from the Philippines, most of them women working as domestics. One reason for this is that Hong Kong's booming economy and the growth of China's economy are both attracting job seekers. For example, the building of Hong Kong's new airport, and all the expressways and other facilities that go with it, is currently the largest construction project in the world. When this airport is finally completed, it will have the capacity to handle 87 million passengers a year. Hong Kong lures people and companies because it is a place where people enjoy fast-rising incomes: earlier this year Hong Kong's per capita GDP surpassed that of the United Kingdom, while in September an international survey rated Hong Kong the fourth most competitive economy in the entire world.

Throughout the nineteenth century and the first half of this century, Hong Kong remained an entrepôt, a service center for the trade between China, the United States, and Europe. Fifty years ago Hong Kong's population was only one tenth of what it is today. After the war, the territory struggled to house millions of displaced persons and to find jobs for them. But with the arrival of Chinese industrialists and entrepreneurs, particularly from Shanghai, Hong Kong began to grow into a manufacturing center.

The rapid growth of Hong Kong's manufacturing industry spurred the growth of the services needed to support it. Hong Kong built its roads and tunnels and port facilities, while banking, securities, retailing, tourism, accounting, communications, real estate, and advertising all came of age. Today, for example, the city is host to more than five hundred banks, including nineteen of the world's top twenty. The only place in Asia with more financial gunpowder is Tokyo. Yet even Japanese banks rely heavily on Hong Kong: there are nearly seventy Japanese banks that use it for much of their offshore banking.

Hong Kong, meanwhile, has been the prime catalyst in unleashing the tremendous pent-up energies in southern China. Investment and expertise channeled through Hong Kong over the last decade have helped turn the province of Guangdong, and in particular the Pearl River Delta to the northwest of Hong Kong, into one of the industrial dynamos of Asia. By most measures this area has the fastest-growing economy on earth. In the 1980s it averaged at least 12 percent per year in real terms. Lately it has been expanding at nearly 20 percent per year.

It is almost impossible to overstate Hong Kong's importance to the Pearl River Delta, or to downplay the impact of China's land and labor on the territory. Four out of five Hong Kong manufacturers have moved some of their labor-intensive production across the border, where they now employ many more workers than in Hong Kong itself. In a little noted "reverse brain drain," more than fifty thousand skilled Hong Kong people now work in China, many of them commuting across the border each morning. It is estimated that perhaps a quarter to a third of Hong Kong's currency circulates freely in South China.

Although Hong Kong is minuscule in comparison to China, it is still China's largest source of inward foreign investment and tourist receipts, and more than half the output of China's large and growing economy passes through the ports and trading houses of Hong Kong. Billions of dollars in investment capital flows north through Hong Kong into China: Hong Kong is the biggest investor in China, and China, in turn, is the biggest investor in Hong Kong.

This also helps to explain why Hong Kong has the busiest container port in the world, surpassing Singapore and Rotterdam. In Hong Kong where twenty-two thousand heavy trucks roll across the border from China every day, a twenty-foot container or its equivalent is loaded or unloaded every three seconds. For the same reasons, Hong Kong's airport is now one of the three or four busiest air freight centers in the world—and in a few years, when the first phase of the city's new airport is completed, it may move into the top spot for air freight too.

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It has been suggested in Hong Kong that this is a case of the tail wagging the dog. They like the idea that Hong Kong exerts some control over China's huge economy. Instead it as an acknowledgment that the tail is part of the dog. The reality is that Hong Kong's economy is such an integral part of the economy of China—and especially China's Guangdong Province—that it would take years of surgery to separate the two.

Lately, China's economy as a whole has been rocketing along. Some fear it is expanding too quickly, and there is no doubt that high inflation and changing labor patterns are causing difficult problems in China. So far China's leadership has been able to keep a handle on these problems without having to bring economic expansion to an abrupt halt. It is not easy for them, however, and to some extent what happens in China will have an impact on Hong Kong.

Hong Kong: The Region's Service Center

Even so, Hong Kong has other strengths and ways to minimize the impact of a severe economic slow-down in China, if that should occur. While China's spectacular economic growth has sent sparks into other economies in Asia, most of them have been expanding faster than the West for nearly thirty years. Lately, they have been growing three to four times as fast. And Hong Kong has come of age not only as a gateway to China and its vast resources, but also as a hub for almost all the other swiftly expanding economies of Southeast Asia. Over the last decade or so, Hong Kong has emerged as a regional distribution, marketing, transportation, and financial center for much of Asia, as well as a key part of the global financial market. This is why more companies have their regional headquarters in Hong Kong than in other Asian cities.

Hong Kong, for example, is a regional air traffic hub, and its access to China is unparalleled. From Tokyo you can fly to about five cities in China. Hong Kong has direct air connections to nearly thirty Chinese cities. Hong Kong also hopes to expand its already heavily used port facilities. The new superhighway linking Hong Kong with the major cities of South China is now open, and thousands of workers in China are toiling away to meet the deadline for the completion of a new Hong Kong-to-Beijing rail link. All of this is in preparation for a city which, by the turn of the century, will really be at the heart of a huge metropolitan area of 45 million people—including parts of the Pearl River Delta—and will command even more manufacturing, port, and airport facilities.

Financing this kind of growth is one of the jobs Hong Kong has done exceedingly well. Southeast Asia's sustained high growth rates, as well as its booming consumer markets, have been helped along by the increased investment flows within Asia. Hong Kong is at the center of all this. In addition to its five hundred banks, Hong Kong is host to another two hundred securities and commodity trading companies, numerous investment banks and a fast growing insurance industry making it a large net supplier of funds to Asia. Eight years ago, Hong Kong's banks had about 50 billion US dollars in loans to their customers and other banks outside Hong Kong. Today that overall lending is well above 500 billion US dollars—an increase of nearly 1,000 percent.

But the art of making a deal, of finding a way to structure big financings, of arranging for debt issues—these skills are also among the strong points of Hong Kong's financial community. Hong Kong is the principal center in Asia for packaging large loans which can be syndicated throughout the world, and Hong Kong's merchant and investment banking houses have underwritten billions of dollars in debt and equities in recent times.

It is a reflection of Hong Kong's regional role that more than half the volume on its stock market is in other currencies. Hong Kong has also made its stock market the principal conduit for mainland Chinese companies seeking access to much-needed foreign capital: almost all the Chinese companies that have issued shares outside China have done so through Hong Kong's stock exchange.

Hong Kong is also a regional communications center. Some 450 major corporations and businesses rely on the city for communications. Indeed, Hong Kong is one of the few places in the world which enjoys a fully digital telephone network, while much of the rest of the world uses older technology. This technical sophistication in communications has helped to spur another of Hong Kong's regional roles: Hong Kong is thought to be the largest movie maker in the world outside of Bombay and Hollywood. It is also the telecommunications capital of Asia, a major source of Chinese language TV programming, and the home of a satellite TV network whose broadcasts extend from Saudi Arabia to Vladivostok. If one wants to get a message out to Asia, Hong Kong is a good place to begin.

All of this helps to explain why Hong Kong is among the first cities in Asia where people go if they want to invest in the region, to bank in the region, to advertise to the region, to manufacture within the region, to source products from the region, to ship into or out of the region, to fly elsewhere in the region, to marshal technology for the region, or to manage other businesses in the region.

Hong Kong's "Competitors"

It has been suggested that the rebirth of Shanghai will cut into Hong Kong's business. Shanghai is rapidly building up its financial service sector, and the city's re-emergence as a major commercial center should not be downplayed—it is real and impressive. But the primary market for its skills is the Chinese domestic market—a huge market in its own right, particularly since foreign banks in China are not yet permitted to take deposits or deal in the Chinese currency, but Hong Kong will continue to serve as Southeast Asia's international and regional banking center.

Singapore, on the other hand, has been nipping at Hong Kong's heels for years. It already has a larger foreign exchange market than Hong Kong, and lately has begun to snare some of the listings business of mainland Chinese companies, taking them away from Hong Kong's Stock Exchange. Singapore, too, ranks among the most competitive economies in the world. And its numerous and wealthy overseas Chinese families are also investing in China and elsewhere in Asia, including India.

Singapore, however, lacks the financial and service depth of Hong Kong, and though competition stimulates the city to retain its position, it is not a major competitor in the areas where Hong Kong is a leader. Certainly, for conducting business in or with China, Hong Kong is—and will remain—the place to start.

Looking Ahead

Yet Hong Kong must face its future, a future that includes its transfer of sovereignty to China on the last day in June of 1997. In some quarters, of course, there is considerable doubt and uncertainty about what this change will mean. And it is no secret that Britain and China have had some disagreements about changes in the Territory's electoral system and about the financing of the new airport.

However, as 1997 draws closer, it is worth reminding ourselves of the key principles that underpin China's resumption of sovereignty over Hong Kong, because even now they are not widely understood. China agreed a decade ago that Hong Kong's capitalist way of life and institutions should be allowed to continue untouched for at least fifty years. China likewise agreed not to change Hong Kong's free port status or legal system. Hong Kong will continue to levy it own taxes, retain its revenues, and maintain its own currency without exchange controls after 1997. These principles are enshrined in the Sino-British Joint Declaration and the Basic Law, which will become a constitution for Hong Kong.

Chinese leaders continue to make clear that they regard Hong Kong as a very important outlet for China's economy and as a source of capital and technology and expertise. They need Hong Kong's financial muscle and managerial skills. It is, to some extent, the goose that lays the golden eggs for them, and they do not want to endanger it.

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If China regards Hong Kong as a golden goose, the Chinese leaders also feel that this goose should be kept in good condition. Time and circumstances could, in theory, see a diminution of Hong Kong's economic role. China could try to shift it to Shanghai or elsewhere, but it would take them years to reproduce the financial, manufacturing, shipping, and technical expertise Hong Kong has amassed over decades. China will not want to spend time and resources replicating a city which will soon be part of China anyway: they want to inherit a Territory in good financial shape. Hence the protracted debate about the long-term financing of Hong Kong's new airport. Nor does China wish for a political system in Hong Kong which, though it enfranchises more voters, Chinese authorities feel is a radical departure from what was agreed in the Joint Declaration and the Basic Law. They have made it clear they are not willing to accept the constitutional changes introduced by the Governor, Chris Patten. Public opinion polls show that Hong Kong people are divided on the question of electoral reform, but that many think it is important to learn to work with China, much as Hong Kong has already learned—with conspicuous success—to work with China in economic terms.

For Hong Kong, learning to work with China on other terms is indeed a necessity, and it will assure its place in the region for many years to come. For after all, despite its high operating costs, its strong inflation, and its labor shortage, Hong Kong remains among the first cities in Asia where people go in order to do business throughout the region. Asia is growing, expanding, and moving ahead. Hong Kong will remain the focal point for Asia, as well as the major gateway to China.