

*Conference on "Hong Kong's Past, Hong Kong's Future:*

*More Than An Economic City" organised by*

*Hong Kong Policy Research Institute, Civic Exchange and SynergyNet*

## **Hong Kong of China, Hong Kong of the World**

Tsang Shu-ki

Professor

Department of Economics

Hong Kong Baptist University

[www.hkbu.edu.hk/~sktsang](http://www.hkbu.edu.hk/~sktsang)

15 September 2003

### **Abstract**

Hong Kong's unique characteristic as a metropolitan city lies in a strange mix of "Chinese-ness" and international qualities. Both strengths and weaknesses stem from it. Colonial constraints, the "transition syndrome" and influences of western neo-conservative ideologies have combined to generate short-termism or minimalism in politics, economics and social developments, the consequences of which Hong Kong is still suffering. On the other hand, the resilience of the population was amply demonstrated in the courageous and disciplined responses to the SARS outbreak, as well as the historically civilised (some would say very Chinese) July 1 rally. While losing part of its locational edge in a further opening China, Hong Kong still enjoys a good deal of "quality advantage" over the Mainland, with which it is increasingly integrated as a result of geo-economic forces. Nevertheless, the problems of the underdevelopment of the political elite and the heterogeneity of ideologies within the population have also been obvious. To a large extent, they explain local systemic instability, policy swings, and the paucity of widely shared visions about the SAR's future.

In the author's view, Hong Kong's long-term success hinges on whether it can harmonise the two often conflicting traits of "Chinese-ness" and international qualities, free itself from the shackles of the past and, in the process of collectively redefining its position, truly live up to the image of the SAR as "Hong Kong of China, Hong Kong of the World". That is a tall order, which requires far-sightedness and sagacity. The alternative would be a secular decline of one of the greatest cities of modern history.

# 中國的香港 世界的香港

曾澍基

香港浸會大學經濟系教授

[www.hkbu.edu.hk/~sktsang](http://www.hkbu.edu.hk/~sktsang)

## 摘要

「中國屬性」和國際素質的奇怪混合形成了香港作為大都會的獨特色彩。優勢、弱點都源於此。殖民地制度的規限、「過渡綜合症」、加上西方新保守浪潮的影響，使香港在政治、經濟和社會的發展出現短期行為或「最低度主義」的流弊；其負面後果仍然困擾特區。另一方面，市民處理逆境的韌力，充份地表現於對非典型肺炎疫潮勇敢而成熟的反應，以及非常文明（一些人士會認為極具中國特色）的七一集會。雖然中國進一步的開放使與它經濟關係愈益密切的香港失去部分的地理優勢，特區相對於大陸其他地域，素質還是領先。然而，本地政治精英的發育不足和民眾意識形態的紛紜却頗為明顯。這些因素帶來了系統性的不穩定、政策搖擺、以及對特區未來廣泛共識的缺乏。

作者認為，香港的長期成功取決於它能否調和「中國屬性」和國際色彩之間所經常產生的矛盾，從過去的歷史枷鎖釋放自己，並且在集體地重新定位的過程中，真正實現特區作為「中國的香港、世界的香港」的構想。任務艱巨，港人須具聰慧遠見。否則，現代史上最偉大的城市之一，將步入下坡。

# Hong Kong of China, Hong Kong of the World

## 1. Introduction

The post-1997 era in Hong Kong as a “special administrative region” (SAR) turns out to be a rough ride for the local population. Economically, there has been very little to cheer about. Indeed, crisis followed crisis and we had already seen two recessions before the SARS outbreak struck in the spring of 2003. The tolerance of the citizens was tested to the limits: and the result was the historic rally on July 1. It served as a very clear expression of frustration against an inept government. Further political instability has been avoided lately by the central government’s economic support measures. Can Hong Kong now successfully weather the storm? It remains to be seen.

Hong Kong is no doubt a great metropolitan city with unique characteristics, thanks to the hard work of generations of migrants and the locally born. From a manufacturing hub to an international financial centre, Hong Kong has been an economic success story. Blessed with a wonderful natural landscape and arguably the world’s densest concentration of man-made illuminations, Hong Kong beats New York, London and Tokyo as a place where one can at the same time enjoy the most advanced output of modern civilisation and relax in the arms of Mother Nature.

But the most enchanting element of Hong Kong must be the strange mix of “Chinese-ness” and international qualities, which no visitors will fail to notice. It can be found in shops and restaurants just a few blocks off the Nathan Road in Kowloon, in the ways that Hong Kong enterprises conduct businesses, and in every venue ranging from the classroom to the courtroom. Moreover, the strategic location of Hong Kong as the doorstep to an economically burgeoning China will cast aside any lingering doubt.

Hong Kong has thrived as an interface between the East and the West. The 1997 transition and the recent troubles have however led many to wonder if that sort of position could be kept forever. Integration with the Mainland, for example, might mean a submergence of Hong Kong into the latter’s geo-economic map and a loss of identity for the SAR. Some would argue that this is the only way forward and constitutes nothing to fear about.

It depends on one's perspective. As a Chinese, I can thoroughly accept a relocation of resources, as well as prosperity, among Chinese cities, if the whole country benefits from it. History is full of examples of the rise and fall of cities, including great ones. Yangzhou in China, Venice and Naples in Italy, and more anciently Ephesus in Turkey, are perhaps the most famous among the losers. Nevertheless, my view is that a good deal of developmental assets, both tangible and intangible, has been accumulated in Hong Kong. They belong to the people of Hong Kong and of China. It would be a tremendous waste if we let these assets be squandered, or less than fully utilised in the process of regional economic realignment.

Compared with other competing metropolises, Hong Kong is the most "Chinese" in style and substance. In contrast to other Chinese cities, Hong Kong is the most "international" in outlook and practice. This is the core of our advantage: and we neglect it at our own peril.

## **2. The road to the present crisis**

Hong Kong is in a crisis, which has its historical roots. Constraints that were inevitably imposed on a colony, the "transition syndrome" of 1997, and influences of western neo-conservative ideologies which form a convenient countervailing force against "communism", even though a reforming one, have all combined to generate short-termism and minimalism in politics, economics and social developments, the consequences of which Hong Kong is still suffering.

(1) Colonial constraints: Caution was always the key in governing a colony. Balanced budgets, monetary stability, and the avoidance of long-term commitments constituted the key elements of sound economics. The long period leading to the political transition of 1997 only aggravated such an innate tendency. The need for confidence boosting measures after the 1989 turbulence in China was the exception.

(2) The "transition" syndrome: The lengthy political transition, coupled with wrangling between the Chinese and British governments, also dampened any major initiatives that the Hong Kong administration could take in the pre-1997 period with regard to institutional reforms, economic restructuring and upgrading, and social empowerment. The Chinese were suspicious of any policies which might result in a "squandering" of Hong Kong's valuable reserves or resources; while the British

apparently had little incentive other than winning the war of political publicity. The motto of the time seemed to be: “the less change, the better”, and most were preoccupied with making quick money while “the good time” lasted.

(3) Neo-conservatism: Reaganism and Thatcherism of the 1980s led to a worldwide shift to the right in politics, economics and ideologies. Being a metropolitan city populated largely by migrants from the Mainland and their descendents, Hong Kong was easily influenced. The younger elites were very much disposed towards western thinking, with relatively little understandings about the sea change on the Mainland. Many of the elder generations were die-hard anti-communists. *Laissez faire* and libertarianism found echo in the heart of most. The aftermaths of 1989 and the uncertainty surrounding the 1997 transition only heightened the suspicion towards local government interventions and Beijing-sponsored moves.

These factors joined force with two other major developments, which had been driving the local economy since the early 1980s. The first was the “China factor”: Hong Kong's “integration” with Mainland China. The second was the escalating dominance of the property sector. Both factors pushed Hong Kong down the path of what I described as “Manhattanization” (Tsang, 1994). Between 1980 and 1997, the share of the manufacturing sector in GDP dropped from 23.7% to less than 7.0%, while the number of manufacturing workers fell from over 900,000 to below 300,000. During the same period, major service sectors had their employment more than doubled.

Such a process not only brought huge adjustment costs to local labourers. It was in my view not consistent with the framework of “one country, two systems”, under which Hong Kong is not supposed to “merge” itself into the Mainland economy and become “just another Chinese city” (Tsang, 1998b). As stipulated in the Basic Law, Hong Kong is to take care of its own fiscal, monetary and manpower problems. Hong Kong is not supposed to expediently “export” difficulties such as unemployment or the lack of demand for its goods and services to Mainland China, like what New York in the US or London in the UK can do to the rest of the country. Hence the Hong Kong economy should maintain some “coherence” of its own (Tsang, 1994, Tsang and Cheng, 1996).

Unfortunately, these economic constraints of “one country, two systems” were not well understood before 1997. The market was having a “free run”. Even worse, as said, the Chinese and the British sides were submerged in hostile politics. The

consequence was a paralysis of initiatives that could facilitate re-structuring in the appropriate direction. The failure by the Hong Kong government to build up a land bank and to provide an adequate supply of land to the market, as a result of political constraints and the lack of coordinated efforts, was particularly destabilising (Tsang, 1998a).

The local “locomotive” was taken up by the real estate sector and its related businesses. Property prices and rentals surged. Take the example of residential property, their average price level rose by eight folds between 1985 and 1997, yielding an annual compound growth rate of 19.0%, markedly above those of nominal GDP (13.5%) and nominal per capita GDP (11.8%). In many categories of property, Hong Kong had become the most expensive in the world by 1997. As property prices and rentals reached for the sky, the profitability of the real estate sector and its affiliates, e.g. legal services and finance, increased handsomely, unwittingly squeezing that of other services (e.g. shops and restaurants), not to mention manufacturing industries which were further pushed out of Hong Kong.

Being agitated yet tired, an economy is vulnerable to speculation. The narrowing of the range of profitable activities forced people to put money into an already shrinking “funnel”. It was like a scenario of “too much money chasing too few profitable opportunities”. Ironically, by design or by default, the China factor also directly fuelled the financial bubble in Hong Kong. Huge amounts of Chinese capital reportedly poured into the property and stock markets in the territory in the run-up to 1997.

Even without the Asian financial crisis of 1997-1998, the mode of growth in the Hong Kong economy was not sustainable. The crisis only aggravated the unavoidable corrective downturn, exposing all the problems that had accumulated since the mid-1980s (Tsang, 1999).

### **3. The political entropy**

Economic misfortune notwithstanding, Hong Kong is apparently suffering from a social and political anomie. Foreign visitors must have wondered where else in the world they could find a political leader as abused by the media and the populace as Mr. Tung Chee Hwa. In an authoritarian regime, people dare not criticise; whereas in a parliamentary democracy, the ruling party at least has some support and the opposition is more inhibited by the rule of the game.

Due to the colonial past and the transition syndrome, Hong Kong is unfortunately locked in a half-baked “semi-democracy” faultily designed in the pre-1997 era of suspicion, and governed by an increasingly battered leadership. Under the “executive-led” political system, people have had few ways to ventilate their misgivings and anger about the economic avalanche besides insulting the top echelon of the government. With vested power but little local political support, the latter has reacted by behaving almost randomly. Ideas and slogans rambled from “long-term planning” to “proactive market enabling” to “big market, small government”; swayed between “Hong Kong as Asia’s World City” and “Hong Kong as the Dragon Head of the Pearl River Delta”, and hesitated in facing high-technology innovation and “local community economy”. Meanwhile very little has been effectively done.

Into Mr. Tung’s second term, the political leadership started to show signs of entropy. In lieu of a change of the peg, Mr. Tung emphasised the importance of restoring competitiveness by cost and wage adjustments, while one of his ministers put forth “nine measures” to “stabilise” property prices (actually to move them slightly up). An obviously grateful property tycoon admitted that only five or at most seven of those largely administrative measures would have been sufficient---which turned out to be one of those “predictions” with little empirical ground. Mr. Tung reportedly wrote his January 2003 Policy Address with the help of only a few aides. He talked about the need for Hong Kong to become a knowledge-intensive economy, and the priority of investing in education, but another of his ministers promptly proceeded to plan deep cuts in university and post-secondary funding.

Lack of concrete visions and the ability in implementation apart, policy swings in the SAR government are in my view a reflection of the heterogeneity of ideologies in Hong Kong. Such heterogeneity was a historical product; but the local socio-political system has not provided any useful mechanism in resolving it and in facilitating consensus formation. In the pre-1997 years, social researchers discussed the issues of “ambivalence” among local citizens concerning their attitudes towards the Beijing authorities, which showed both noted reservations and yet surprising deference. My suspicion was: the surveys that they carried out might have caught a “split sample”---indeed one split in multiple ways. Hostility and deference were actually expressed by different subgroups of respondents.

In any case, policy swings themselves are hardly beneficial to the emergence of widely shared views. Every party can claim that its advocacy or policies have not really been adopted by the government and therefore tested in reality. Hence no position is verified or rejected by history. This contributes to the general loss of direction for Hong Kong's development.

#### **4. Two views of Hong Kong's economic future**

The Policy Address by Mr. Tung Chee Hwa at the beginning of 2003 was in essence an economic manifesto. The central message was that Hong Kong should strengthen its ties with the Mainland, especially the Pearl River Delta. Nevertheless, under the guiding philosophy of "big market, small government", what the government could do was to concentrate on reducing the barriers to cross-border flows of resources, and to "open up the circulation within the network".

I am sceptical of the perspective that apparently underpins the SAR Government's present economic policy---the "resource flow" view (「要素流動論」), which has probably been reinforced by the flurry of supporting economic measures launched by the central government in the light of the current political problems. It can be contrasted with the view of "local advantage" (「本地優勢論」). Because of the rapidly emerging competition among Chinese city economies, the resource flow perspective, if not cast in the proper context, is short-sighted as it fails to realise that the enhancement of the freedom and efficiency in the flows of factors of production is a "two-edged sword" (Tsang, 2003a). As Paul Krugman puts it in his *Geography and Trade* (Krugman, 1991), under the trend of globalization, high-grade factors would only converge to cores or centers with economies of scale, industrial clusters, and large and substitutable labour pools.

Of course, if Hong Kong and the Mainland cities strengthen their exchanges of resources, the SAR's implicit and explicit costs of being "caged" under the "one country, two systems" framework could be reduced. Hong Kong may also benefit from an enlargement of business opportunities, just as the "Closer Economic Partnership Agreement" (CEPA) and measures like relaxing restraints on Mainland tourism to Hong Kong are intended to generate. These developments should be welcome; and so far the short-term effects seem rather favourable. Moreover, increasing resource flows is relatively easy, in the sense that it basically involves policy changes that aim at removing existing barriers and constraints.

On the other hand, upgrading technology, developing frontier industries, and promoting competitiveness are much more difficult tasks. Hence in the longer run, the lopsided dependence on Mainland-Hong Kong economic integration may again soften Hong Kong's resolve to tackle the crux of the problem: Hong Kong's lack of cutting edge. The disappearance of the economic boundary could in theory result in a net inflow or a net outflow of resources of different qualities: it is "a blessing or a curse", depending on how the challenges are handled. Without persistent efforts in maintaining local advantage, the consequence could be the SAR's secular decline, as a net load of low-quality factors precipitates in it. The brightest would find much greener pasture in the north.

Hong Kong must therefore reinvent its own niche in the new dynamic circumstance. In my previous writings (e.g. Tsang 2003a), I made the distinction between locational and quality advantage. Hong Kong is losing its locational edge as China continues with its process of economic opening. However, as shown in the recent outbreak of atypical pneumonia, Hong Kong still holds quite a good deal of quality advantage, especially that related to credibility. There is as yet a marked "credibility asymmetry" between the Mainland and Hong Kong. That is why Mainland tourists and businessmen like to purchase gold and jewelry, cosmetics and expensive drugs etc. in the SAR.

## **5. Hong Kong to become the Switzerland of Asia?**

To make full use of that kind of advantage, I would argue that Hong Kong should aim at becoming the "Switzerland of the Asian-Pacific region"---a view which Mr. Wang Zhan, the chief policy advisor to the Shanghai Municipal Government actually expressed during his visit to the SAR in 2002. Successful small open economies like Switzerland, Denmark, and Finland have all adopted a highly focused strategy of concentrating on taking the lead in a few frontier industrial and service sectors. In this regard, a particular example serves to illustrate the potentials and the obstacles that lie ahead of us: that of developing a pharmaceutical industry.<sup>1</sup>

---

<sup>1</sup> Besides drugs making, Hong Kong can promote other industries that are closely associated with credibility: e.g. different fields of biotechnology, high-security financial and commercial service, sophisticated software technology, and material sciences applications. As for creative industries, cultural and entertainment software etc., for which credibility is not a crucial element, the SAR also has quality advantage.

Hong Kong appears to be an excellent place to promote the techniques of combining Chinese and western medicine, as knowledge of both sides meets here. The SAR is close to the sources of materials and the vast markets for the end products, and as said, it possesses a relatively high degree of credibility. Nevertheless, drugs manufacturing represents a high-risk adventure. The rule of thumb is that a marketable drug would require ten years of efforts over 6,000 experiments, and an average investment of US\$1 billion. So government's involvement or assistance in the initial stage is an important condition for the industry's eventual take-off.

Singapore is an outstanding example. Resorting to various forms of incentives (including preferential tax treatments, affordable space in technology parks built by the government, R&D funding and benefits, start-up capital provision and matching etc., to the tune of billions of US dollars), the Singapore government has been able to help launch the pharmaceuticals industry, which has become the island republic's third largest exporter behind the petroleum and electronic sectors. Several world-class drugs manufacturers have invested and set up plants in the country. In 2002, pharmaceutical exports grew by nearly 60%, amounting to 4.7 billion US dollars.<sup>2</sup>

To compete with Singapore on this front, Hong Kong needs a good deal of efforts and coordinated measures. Besides CEPA with the Mainland, the SAR Government should proactively negotiate with foreign countries in Europe, America, and Asia for free trade agreements (FTAs) that reduce tariff and non-tariff trade barriers, particularly the latter concerning high-tech products and services.<sup>3</sup>

---

<sup>2</sup> For a report of the pharmaceuticals industry in Singapore, see "Little Island, Big Pharma", *Business Week*, 17 February 2003, p.24. Regarding the developments of its biomedical sciences (including basic characteristics, the recent trends, and the government's preferential policies and measures), visit the website <http://www.biomed-singapore.com/bms/index.jsp>, or alternatively, see the details on the website of the Economic Development Board at [http://www.sedb.com/edbcorp/sg/en\\_uk/index.html](http://www.sedb.com/edbcorp/sg/en_uk/index.html). The official goal is to turn Singapore into the "Biopolis of Asia".

<sup>3</sup> Singapore has already entered into free trade agreements with New Zealand, Japan, Australia, EFTA and the US. It is negotiating with Mexico, Canada, ASEAN, China and South Korea. See the official web page of its Ministry of Trade and Industry: [http://www.mti.gov.sg/public/FTA/frm\\_FTA\\_Default.asp?sid=27](http://www.mti.gov.sg/public/FTA/frm_FTA_Default.asp?sid=27). On a list of free trade agreements in the world, see "Frequently Asked Questions: FTAs" at [http://www.mti.gov.sg/public/FAQ/frm\\_FAQ\\_Default.asp?sid=2&did=33&cid=113](http://www.mti.gov.sg/public/FAQ/frm_FAQ_Default.asp?sid=2&did=33&cid=113)

If Hong Kong fails to enhance the quality and credibility advantage that it still holds, so as to create sustainable cores of relatively high growth for the economy, the intangible assets that it has accumulated (including goodwill) will drain off. Its economic prospect will be worrisome.

## **6. Hong Kong's economic prospects**

In more practical terms, the Hong Kong economy is being confronted with three types of serious challenges.

(1) Uncertainty of SARS as a special shock: Unlike an earthquake, the chance of recurrence may be relatively high. Will a “second wave” emerge this winter? Will there be other deadly viruses in a “40-year epidemiological cycle” as feared by some medical experts? How can we “insure” against such a risk?

(2) “Downwave”: Serious downturn of the advanced economies led by the US may unfold, impacting adversely on Hong Kong. The US seems to be facing unprecedented hurdles, as the rebound is unusually lacking in energy (particularly regarding job creation) even after 13 rounds of interest rate cuts that resulted in 45-year lows and significant fiscal stimulus in the form of President Bush’s tax cuts (which few would dispute constitute “one of the most stimulative combinations of monetary and fiscal policy in history”) (Tsang, 2003b). The huge amount of liquidity has gone mainly to the financial and housing markets, which are in the danger of drastic corrections. Despite Hong Kong’s increasing reliance on the Chinese market, how could it deal with the repercussions of a possible worldwide stagnation?

(3) Structural transformation: The development of Hong Kong into a “knowledge intensive” economy in the aftermath of the pre-1997 bubble and in face of keen inter-city competition from the Mainland turns out to be rather troublesome.

Of the challenges, the first two are highly uncertain and largely out of our control. Addressing the third requires patience and consistent effort. Although we have to care about irreversibility in economics, e.g. bankruptcy and destruction of assets, and hence some relief measures are necessary, normal counter-cyclical policies could be ineffective, if not a waste of resources given the current political climate and governance structure. In the eagerness to buttress Hong Kong’s politics through economic means, the SAR might also ask for, and the central authorities

might agree to, more economic support measures that bring short-term rather than long-term benefits.

## **7. Concluding remarks**

So my overall plea is for caution and far-sightedness. We should take into full account the difficulties and our capabilities, and formulate responses with calmness and vision. To maintain the status of the SAR as the country's leading metropolitan city with a genuinely worldwide perspective, our destiny lies with harmonising our two conflicting traits of "Chinese-ness" and international characteristics. The mix is actually our unique niche, and we should harness it to our benefit. Alternatively, we could become just "another Chinese city"---in a process of "free" cross-border resource flow in lieu of local hard work in achieving global excellence.

We might perhaps take clues from I Ching: after falling from the sky, we better behave like a "low-lying and nurturing dragon" instead of a "flying" one again any time soon. In other words, economic policies should focus on re-building long-term strengths, on the basis of Hong Kong's "quality advantage", rather than just alleviating short-term pain. An Economic Development Authority funded basically by bonds and sheltered from messy annual budgetary politics would be one of the important options to turn Hong Kong into a future "Switzerland of Asia".

Of course, the pre-requisite for a successful future is not just economic in nature. The local polity must overcome the problems of the underdevelopment of elite and the heterogeneity of ideologies, and release itself from the shackles of the past. Without a more popular and hence more stable vehicle of policy formulation and implementation, it will be very difficult to take a firm stance on long-term endeavour. Let history be history, and let us look forward.

## ***References***

Krugman, Paul (1991), *Geography and Trade*, Leuven University Press and MIT Press.

Tsang Shu-ki (1994), "The Economy", in *The Other Hong Kong Report 1994*, Hong Kong: The Chinese University Press, pp.125-148.

Tsang Shu-ki and Cheng Yuk-shing (1996), “The Economic Link-up of Hong Kong and Guangdong: Structural and Developmental Problems”, July, article posted on author’s website [www.hkbu.edu.hk/~sktsang/Tsang9607.doc](http://www.hkbu.edu.hk/~sktsang/Tsang9607.doc).

Tsang Shu-ki (1998a), "Handling Credit Crunch under Hong Kong's Currency Board System", article posted on author’s website: [www.hkbu.edu.hk/~econ/web987.html](http://www.hkbu.edu.hk/~econ/web987.html).

Tsang Shu-ki (1998b), “The Hong Kong Economy in the Midst of the Financial Crisis”, keynote speech, *Regional Conference on the Financial Crisis*, Hong Kong Journalists Association, 26 September: [www.hkbu.edu.hk/~sktsang/web9810.html](http://www.hkbu.edu.hk/~sktsang/web9810.html).

Tsang Shu-ki (1999), “The Hong Kong Economy: Opportunities out of the Crisis?” *Journal of Contemporary China*, vol.8, no.20, pp.29-45.

Tsang Shu-ki (2003a), “Hong Kong’s Economic Strategy Reconsidered”, 7 April, article posted on author’s website [www.hkbu.edu.hk/~sktsang/Devt\\_Strategy\(e\).doc](http://www.hkbu.edu.hk/~sktsang/Devt_Strategy(e).doc).

Tsang Shu-ki (2003b), “Long Waves: An Update”, 30 July, article posted on author’s website [www.hkbu.edu.hk/~sktsang/Long-WavesUpdate.pdf](http://www.hkbu.edu.hk/~sktsang/Long-WavesUpdate.pdf).