SUSTAINING HONG KONG'S SERVICES AMID CHANGING DYNAMICS OF GREATER CHINA ECONOMIC LINKAGE

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Executive Summary

1. Hong Kong has recently raised concern about its diminishing role as a major service provider between Taiwan and China following the expansion of direct economic linkages across the Strait. Understandably, 94% of Hong Kong's gross domestic product and 88% of its employment were from the service sectors in 2012.

2. Despite this diminishing role, the territory's greater integration with China through trade, financial links and tourism has continued to underpin its service oriented economy. In 2012, China took 35% of Hong Kong's exports and 43% of its imports in services.

3. China is Hong Kong's largest trade partner in transport services, accounting for 17% of Hong Kong's exports and 19% of its imports in 2012. Hong Kong is an important transit hub for China's external trade, especially for the Pearl River Delta region. Its greater international flight options compared to those of Shenzhen and Guangzhou have made it an essential gateway for mainland travellers going abroad.

4. The quick catching up of mainland cities in transport services will propel Hong Kong to discover other higher value-added service sectors. Its free port status, efficiency and better infrastructure connection with the Mainland complements rather than competes with its neighbouring mainland cities in transport services.

5. The tremendous business opportunities from China's financial reform however could not unseat the US and the UK as Hong Kong's top trade partners in financial services, accounting for 25% and 17% of its exports and 11% and 16% of its imports respectively in 2012. Meanwhile, China only took 3% and 6% of its export and imports in financial services.

6. Hong Kong's greater financial connection with the West (eg. large trade figures in financial services, Hong Kong dollar's peg to US currency and a great amount of Hong Kong financial assets in US dollar) has made the territory's financial sectors vulnerable to any potential crisis from the West.

7. China’s deregulation of mainland visitors to Hong Kong under the Individual Visit Scheme since 2003 has contributed to Hong Kong’s bulging trade surplus in travel. In 2012, China accounted for 75% of Hong Kong’s exports and 30% of its imports in travel services.

8. In 2013, Hong Kong received 54 million visitors, of which 75% came from the Mainland. The visible business profit from mainland visitors’ spending in the territory could not however ease growing tension between the Mainlanders and Hong Kongers.

9. Hong Kong’s service economy will continue to prosper in the near term with China’s continuous grant of preferential treatment. In the long run, strengthening Hong Kong’s bridging role between mainland China and global market will be crucial for the viability of its services.

10. Hong Kong’s strength in financial services could enhance China’s links with regional economies in financial terms. Its participation in the Trans-Pacific Partnership would serve to further develop China-US relations.