

Press release

HONG KONG LOSES “BEST BUSINESS ENVIRONMENT” SPOT

Hong Kong will lose its position as the Asia-Pacific’s best location for doing business, falling just behind rival Singapore while the region as a whole struggles to keep pace with reforms being made by other countries world-wide. According to the Economist Intelligence Unit’s latest quarterly Business Environment Rankings - an authoritative forward-looking survey of 70 factors affecting operating conditions, from government policy to access to capital - Asia will continue to have a markedly worse business environment than Western Europe or North America during 2002-06.

The operating environment in Hong Kong remains “very good” the highest qualitative assessment provided by the rankings. But its score slips compared with the 1997-2001 historic period, pulling down the SAR from fifth to 11th place out of 60 countries covered by the rankings. (In the previous Business Environment Rankings, Hong Kong was in ninth place for the forecast period.) Singapore, previously second in Asia, moves into first place regionally. “Hong Kong is trying to walk forward, but others are running,” said Graham Richardson, Asia Regional Director for the Economist Intelligence Unit.

This fall in the rankings coincides with a structural change in the rate of GDP growth in the Hong Kong Special Administrative Region (SAR). Economic growth will be boosted during the early part of the 2002-06 forecast period by the recovery of the world economy from the downturn of 2001, reaching a forecast 1.7% this year and 3.9% in 2003. However, while the SAR will continue to gain from its links to China, the growth of the mainland economy will no longer provide the unadulterated benefits that it seemed to during the last two decades. As the mainland economy liberalises, Hong Kong’s special role as an entrepot for visible trade with China is likely to diminish. As a result, Hong Kong’s average annual GDP growth rate over the next five years is likely to drop to 3.3%. By contrast, in the five years prior to the regional downturn of 1998, Hong Kong’s economy grew by an average of 5% a year.

Key concerns: political effectiveness, openness to competition and labour skills

The loss of trade to cheaper ports in China is just one external risk to Hong Kong’s

continuing competitiveness. On the domestic front there are also causes for concern. In the latest survey, Hong Kong loses the most ground in its scores for political effectiveness and for policy towards private enterprise and competition. These fall 9.2% and 9.8% respectively, against the 1997-2001 comparison period. Worsening civil-service morale and the uncertain impact on policymaking of chief executive Tung Chee-hwa's new "accountability" system of political appointees contributed to the drop in the political-effectiveness score for 2002-06. Continuing concern over the government's cosy relationship with certain sectors of the business community, combined with lack of progress in developing a competition law, were among the causes of the expected decline in the competitive environment for businesses.

The quality of the workforce - in particular, the ability to adapt to the new skills required in a knowledge-based economy - also remains a major worry. The SAR's overall labour market score falls 8% between the historic and forecast periods, reflecting concerns over the education system and poor standards of English. "Shortages of highly skilled labour will be an endemic problem as Hong Kong seeks to move up the value chain, said Richardson.

Still one of the world's freest economies, though

Not all the news is bad. "Hong Kong starts from such a competitive position that a slight slippage is hard to prevent," said Richardson. Hong Kong still has, for example, the world's most liberal regimes for taxation and for foreign trade and exchange controls, a fact reflected in its continued No.1 world ranking in both categories. Another rankings category, market opportunities, shows a substantial improvement over the comparison period, with Hong Kong's score advancing nearly 15% on the back of the increased opportunities, particularly in services, anticipated as a result of China's entry to the World Trade Organisation (WTO). But scores are improving faster for countries elsewhere.

Singapore on top

Singapore will pip Hong Kong at the post to become Asia's most attractive place to do business. It, too, is struggling to upgrade its business environment as rapidly as countries elsewhere, and slipped two places in the world-wide rankings. In the latest survey, the city-state overtook Hong Kong in two categories - policy towards private enterprise and competition, and the labour market - and improved its standing relative to the SAR in five other categories, either extending its own lead or narrowing Hong

Kong's advantage. Hong Kong's lead in having a liberal and uncomplicated tax regime also may be eroded as the Hong Kong government considers broadening the tax base to reduce the structural budget deficit; Singapore's government, in contrast, enjoys a much stronger underlying fiscal position, enabling it to consider cuts in both corporate and personal income tax.

In the rest of the region, only India, the Philippines, South Korea, Sri Lanka and Thailand climbed the global rankings. The relative world positions of the other 11 Asian and Australasian countries covered either worsened or were unchanged. The Hong Kong SAR was one of only three countries worldwide whose absolute scores for 2002-06 deteriorate compared with the previous ranking period of 1997-2001.

What are the EIU Business Environment Rankings?

The EIU has developed a global business rankings model, which is applied to the world's 60 largest countries, and seeks to measure the quality or attractiveness of the business environment and its key components. The model considers 70 factors which affect the opportunities for, and hindrances to, the conduct of business in each country. The resulting scores allow us to rank the countries in order of attractiveness to business. The model is used to generate scores and rankings for the past five years, and also for the next five years (using EIU forecasts and assessments of likely business and political developments).

About the Economist Intelligence Unit

The Economist Intelligence Unit, the business-to-business arm of The Economist Group, publisher of The Economist, is the world's leading provider of country intelligence, with over 500,000 customers in corporations, banks, universities and government institutions. Our mission is to help companies do better business by providing timely, reliable and impartial analysis on worldwide market trends and business strategies. Through our global network of over 500 analysts, the EIU continuously assesses and forecasts political, economic and business conditions in 195 countries, and provides insight into how companies are responding.

Overall regional scores

	1997-2001 Total score (out of 10)	2002-06 Total score (out of 10)
North America	8.63	8.71
Western Europe	7.64	8.10
Asia & Australasia	6.33	6.88
Latin America	5.71	6.28
Eastern Europe	5.31	6.27
Middle East & Africa	4.92	5.76
World average	6.33	6.96

Business environment rankings

	1997-2001 Total score (out of 10)	Global rank (out of 60)	2002-06 Total score (out of 10)	Global rank (out of 60)	Change in total score	Change in rank	Qualitative assessment 1997-2001 ^a 2002-06 ^a	
Australia	7.83	15	8.23	15	0.40	0	Good	Very good
China	5.31	42	6.05	42	0.74	0	Poor	Moderate
Hong Kong	8.57	5	8.46	11	-0.11	-6	Very good	Very good
India	5.19	46	6.23	41	1.04	5	Poor	Moderate
Indonesia	5.09	48	5.68	49	0.59	-1	Poor	Moderate
Japan	6.60	26	7.26	27	0.66	-1	Good	Good
Malaysia	6.81	25	6.75	33	-0.60	-8	Good	Good
New Zealand	8.03	12	8.17	16	0.14	-4	Very good	Very good
Pakistan	4.36	52	5.02	58	0.66	-6	Very poor	Poor
Philippines	5.52	38	6.50	35	0.98	3	Poor	Good
Singapore	8.40	7	8.47	9	0.07	-2	Very good	Very good
South Korea	6.35	31	7.27	26	0.92	5	Moderate	Good
Sri Lanka	4.93	49	5.87	46	1.06	3	Very poor	Moderate
Taiwan	7.35	19	8.02	20	0.67	-1	Good	Very good
Thailand	6.27	33	6.35	32	0.58	1	Moderate	Good
Vietnam	4.61	50	5.32	56	0.71	-6	Very poor	Poor

^a Qualitative grades are assigned according to the following scale: very good: score more than 8; good: 6.5 to 8; moderate: 5.5 to 6.4; poor: 5 to 5.4; very poor: less than 5.

Regional rankings

	1997-2001 Regional rank (out of 16)	2002-06 Regional rank (out of 16)	Change in rank
Australia	4	3	1
China	11	12	-1
Hong Kong	1	2	-1
India	12	11	1
Indonesia	13	14	-1
Japan	7	7	0
Malaysia	6	9	-3
New Zealand	3	4	-1
Pakistan	16	16	0
Philippines	10	10	0
Singapore	2	1	1
South Korea	8	6	2
Sri Lanka	14	13	1
Taiwan	5	5	0
Thailand	9	8	1
Vietnam	15	15	0