

For information

**LEGISLATIVE COUNCIL PANEL ON
MANPOWER**

**THE MAINLAND AND HONG KONG
CLOSER ECONOMIC PARTNERSHIP ARRANGEMENT (CEPA)
IMPACT ON LOCAL EMPLOYMENT**

PURPOSE

This note informs Members of the Administration's assessment on the impact of the implementation of the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) on local employment.

BACKGROUND

2. The main parts of CEPA were signed on 29 June 2003, and its six annexes, which set out the implementation details of the Arrangement, were signed on 29 September 2003. CEPA covers three main areas: trade in goods, trade in services, and trade and investment facilitation. Except for the liberalisation measures under the telecommunications sector which have already been implemented on 1 October 2003, the preferential treatments under CEPA for Hong Kong goods and services will come into effect on 1 January 2004. The key features of CEPA are summarized in Annex.

**IMPACT OF IMPLEMENTATION OF CEPA ON LOCAL
EMPLOYMENT**

General

3. The conclusion and implementation of CEPA will bring about unprecedented opportunities to Hong Kong business, trade and service sectors, and greatly enhance economic cooperation and integration between the Mainland and Hong Kong. Preferential and exclusive access opportunities for Hong Kong products and services under CEPA, which are ahead of or beyond the Mainland's liberalization commitments in the World Trade Organisation (WTO), will benefit our manufacturing and services sectors in their expansion into the Mainland market. CEPA will also enhance the attractiveness of Hong Kong to overseas investors. We therefore

anticipate that CEPA will help promote Hong Kong's traditional and emerging industries, facilitate our economic restructuring, and directly and indirectly create employment opportunities.

Expansion of trade in Goods

4. On trade in goods, the zero import tariff preference will render Hong Kong products more competitive in terms of price vis-à-vis those produced by other economies when entering the Mainland market. We believe that this preference will attract to Hong Kong manufacturing of brand name products, or manufacturing processes with high-value added content or substantial intellectual property input, thereby promoting the restructuring and diversification of industries in Hong Kong towards high value-added and high technology.

5. Many of the 273 products currently attract high tariffs. Some specific examples are: articles of jewellery (35%), micromotor for toys (24.5%) and clocks and watches (23%). Though the Mainland has committed to lowering tariff rates in its WTO accession protocol, the committed final bound tariff rates (i.e. after full implementation of its WTO commitments) for some products within the 273 codes will remain at high level (tariffs for some products remain as high as 35%). Zero tariff preference under CEPA will make these Hong Kong products more competitive vis-à-vis those produced elsewhere, and therefore increase the incentive to manufacture these products in Hong Kong. We believe that the sectors concerned are more likely to set up new manufacturing plants in Hong Kong, or increase the manufacturing processes here, and thereby creating more jobs. Separately, according to trade statistics, the 273 items covered in the first phase include many product types in which Hong Kong traded substantively with the Mainland, such as textiles and clothing (HK\$16.7 billion), electrical and electronic products (HK\$2.4 billion), optical and photographic articles (HK\$1.2 billion), plastic articles and paper articles (HK\$4.5 billion). We believe that these sectors also have high potential for production expansion and increasing exports to the Mainland, and thereby bring about employment opportunities in both the manufacturing sector and the related industries such as import and export as well as transportation.

Expansion on trade in services

6. The WTO-plus market liberalisation measures in the 18 services sectors would give Hong Kong service suppliers a “first mover” advantage.

CEPA has great potential to encourage existing businesses in Hong Kong, whether foreign-owned or local-owned, to tap the Mainland market opportunities in such sectors, and in support of the envisaged trade creation and activities, to engage additional staff to manage and run their new or expanded operations in Hong Kong and in the Mainland. In respect of professional services, CEPA allows professionals of Hong Kong to obtain qualifications and to practise in the Mainland. Professional services in Hong Kong are well established and their standards and quality of service are recognized internationally. They should be very competitive in the Mainland market. Additional market access under CEPA will certainly be conducive to improving career prospects and opportunities for professionals of Hong Kong and will indirectly help improve the labour market of staff in support of the provision of professional services.

Tourism

7. Tourism is an important aspect of trade in services under CEPA. Residents of Guangzhou, Shenzhen, Zhuhai, Dongguan, Zhongshan, Jiangmen, Foshan and Huizhou of the Guangdong Province together with residents of Beijing and Shanghai have already been allowed to visit Hong Kong under the “individual visit” scheme. The scheme will be extended to cover the whole of Guangdong Province by May 2004. Since the implementation of the “individual visit” scheme on 28th July 2003, the number of Mainland visitors coming to Hong Kong under the scheme amounted to 290 573 by close of 4 November. This accounted for around 10% of the total number of Mainland visitors during the period. Both the number and their share in total number of incoming visitors from the Mainland surged through the period. An increase in the number of in-bound tourists will certainly benefit Hong Kong’s economy and local employment in tourism and related industries, such as restaurant and retailing.

Investment creation

8. As a matter of fact, Hong Kong’s excellent business environment, simple and low tax regime, cosmopolitan lifestyle, superb geographical location, free economy, rule of law, skilled workforce with international vision, world class infrastructure as well as efficient and clean government are factors attracting many overseas multi-national corporations to set up their regional headquarters or offices in Hong Kong.

9. Building on the above strengths, it is anticipated that the implementation of CEPA will attract even more overseas companies to invest and expand their business in Hong Kong; and thereby create more employment opportunities. Under CEPA, objective and transparent criteria are laid down on what constitutes a Hong Kong service supplier. A service supplier incorporated or established under the laws of the HKSAR and has substantive business operations here can enjoy CEPA treatment, regardless of the origin of its capital. In addition to setting up a new company in Hong Kong, overseas companies and investors can choose to cooperate with business partners in Hong Kong through various routes and means to expand into the Mainland market. They may also merge with or acquire an existing Hong Kong company. All these business and investment activities will inject new impetus to Hong Kong's economy and enhance local employment opportunities. CEPA may also encourage Mainland companies with international aspirations to use Hong Kong as a "springboard" to the world. All the above will have a positive multiplying effect on Hong Kong's economy and employment. Recognizing the importance of promoting CEPA overseas, Government agencies, such as Invest Hong Kong and Economic and Trade Offices overseas, and other HK Inc members, including the Hong Kong Trade Development Council, will be undertaking an intensified and concerted programme of promotional activities outside Hong Kong.

Limitations of conducting a quantitative assessment at this stage

10. As for the specific number of jobs that would be created as a result of CEPA, it depends on how the trade in Hong Kong and overseas, including professional practitioners and enterprises, would like to take advantage of the CEPA benefits to gain greater access in the Mainland market as well as on their professional and business development strategies. This will determine the scale of CEPA-induced business activities, the direct and indirect economic spin-offs, as well as employment opportunities for Hong Kong. As mentioned above, the Administration believes that the implementation of CEPA will have a very positive impact on Hong Kong economy. However, before the implementation of the zero tariff arrangement and the majority of the preferences under services trade on 1 January 2004, any attempt to estimate the effect of CEPA, including its impact on local employment, has to be broadbrush. As this is a completely new arrangement, there is little well-established historical trend data to support assessment of the CEPA-induced impacts in quantitative terms, and even less data to support an assessment at the micro-level. Moreover, the effect of CEPA most likely will be entwined with that of other concurring events and developments. Any

attempt to isolate the CEPA effect will necessarily be arbitrary, based on best knowledge of the relevant industry and the concerned product. Nevertheless, the Government should be in a better position to review the situation some time after the implementation of CEPA when more statistics on trade and other related aspects become available to enable more objective judgment of trends and assessment of its impact on local employment.

RELATED POLICY INITIATIVES

11. To facilitate the restructuring of industries in Hong Kong, the Administration will continue its support to local manufacturing industries. Such support measures include provision of a full range of consultancy services through the Hong Kong Productivity Council; standards and conformity assessment services through the Innovation and Technology Commission; and advisory and information services through the Support and Consultation Centre for Small and Medium Enterprises (SUCCESS) of the Trade and Industry Department. Following the signing of CEPA and its annexes, services provided through SUCCESS have been strengthened with CEPA elements. Amongst other services, a CEPA corner in the reference library has been set up, seminars and workshops on business opportunities arising from CEPA are being organised, free business advisory services on issues related to China trade are available, and a one-stop enquiry point on CEPA-related enquiries has been set up.

12. In addition, the Government supports local industries through comprehensive funding schemes. Four funding schemes for Small and Medium Enterprises (SMEs), with a total government commitment of \$7.5 billion, are in place to help SMEs secure loans to acquire business installation and equipment, enhance human resources, expand markets, and enhance competitiveness. As at 1 November 2003, over 43,000 applications have been approved, involving more than \$3 billion of government guarantee/grant and benefiting more than 24,000 SMEs.

13. To enhance the skills of the local workforce, various programmes are offered by the eight publicly-funded tertiary institutions, the Vocational Training Council, the Clothing Industry Training Authority, the Employees Retraining Scheme, and the Skills Upgrading Scheme.

14. Moreover, to strengthen the overall competitiveness of Hong Kong, the Administration will continue to enhance our internal business environment. We will strive to keep Hong Kong a business-friendly city by keeping our efforts in cutting red tape, in eliminating unnecessary regulations, in reducing compliance costs and in improving government services to facilitate business. In this connection, the Administration has launched the Helping Business Programme with the aim of improving the business environment of Hong Kong and maintaining its position as one of the best places in the world for business. We have so far completed over 100 studies and projects and implemented some 400 helping business initiatives. Many of these initiatives will facilitate traders in setting up and conducting business under CEPA, including:

- Setting up of a business licensing information centre to provide efficient and effective one-stop licensing information services.
- Streamlining of process and provision of one-stop services for business registration. Applications submitted in person can now be completed within 30 minutes.
- Streamlining the Customs cargo clearance requirements of the Customs & Excise Department and enhancing the related services.
- Actively developing e-business, including electronic service delivery for import/export trade declarations, manifests and applications for certificates of origin.
- Streamlining the application procedures for cross-boundary permits of private vehicles

A recent World Bank study shows that Hong Kong is one of the easiest places in the world to set up business, ranking 8th among 133 economies, and 2nd in Asia.

CONCLUDING REMARKS

15. While a quantitative impact assessment of CEPA on local employment is premature at this stage, the Administration believes that CEPA's effect on Hong Kong's economy as well as employment is very positive. The Administration is fully committed to the successful implementation of CEPA and to facilitating the business sector in seizing

new opportunities arising from the Arrangement with a view to revitalizing our economy.

Commerce, Industry and Technology Bureau
12 November 2003

SUMMARY OF THE KEY FEATURES OF CEPA

TRADE IN GOODS

The Mainland has agreed to eliminate tariffs on imported goods of Hong Kong origin by stages. 273 Mainland product codes meeting the rules of origin requirement will enjoy zero tariff starting from 1 January 2004. These product codes cover some electrical and electronics products, plastic articles, paper articles, textile and clothing, chemical products, pharmaceutical products, clocks and watches, jewellery, cosmetics, metal products, etc. For products not covered in the initial phase, the Mainland will apply zero tariff latest by 1 January 2006 upon applications by local manufacturers and upon the CEPA rules of origin being agreed and met.

2. For the 273 Mainland product codes covered in the initial phase, Hong Kong's existing origin rules are adopted as the CEPA origin rules for 187 (68%) product codes. In respect of 48 (17%) product codes for which there are no existing Hong Kong origin rules, the Mainland has agreed to adopt the "Change in Tariff Heading" (CTH)¹ approach as the CEPA origin rules. For the remaining product codes, a 30% value-added requirement will be adopted as the CEPA origin rule. The formula for calculating the value-added percentage will take into account the costs of product development (e.g. design, development, intellectual property rights, etc.) incurred locally, thereby helping to provide more flexibility to our trade and encourage high value-added activities to be undertaken in Hong Kong.

TRADE IN SERVICES

3. On trade in services, CEPA will cover the following sectors:

- management consulting services;
- convention and exhibition services;
- advertising services;
- legal services;
- medical and dental services;
- accounting services;

¹ A "CTH" origin rule means that the products have been manufactured to the extent that their classification in the World Customs Organisation Harmonised System falls in a different four-digit heading from the classification of the non-originating constituent materials used.

- real estate and construction services;
- distribution services;
- logistics, transportation, forwarding and storage services;
- tourism services;
- insurance services;
- banking services;
- securities services;
- audiovisual services; and
- telecommunications services.

4. Broadly speaking, the Mainland's concessions permit earlier access to the Mainland market, ahead of China's WTO timetable, to Hong Kong companies and services providers. In some sectors, such as legal services, banking services, audiovisual services and advertising services, the Mainland's offer will go beyond its WTO commitments.

5. As regards the definition of Hong Kong service suppliers, apart from companies, partnerships, sole proprietorships and natural persons of Hong Kong will also be able to enjoy CEPA benefits provided that they fulfill the stipulated conditions. Generally speaking, natural persons will have to be Hong Kong permanent residents whereas juridical persons will have to be incorporated or formed in Hong Kong and have engaged in substantive business operations in Hong Kong for three to five years. Before applying to the relevant Mainland authorities for the provision of relevant services under CEPA, Hong Kong service suppliers as juridical persons have to first apply to the Trade and Industry Department for a Hong Kong Service Supplier (HKSS) Certificate.

TRADE AND INVESTMENT FACILITATION

6. Agreement to enhance trade and investment facilitation was also reached on the following seven areas :

- (i) trade and investment promotion;
- (ii) customs clearance facilitation;
- (iii) commodity inspection and quarantine, food safety, quality and standardization;
- (iv) electronic business;
- (v) transparency in laws and regulations;
- (vi) cooperation of small and medium enterprises; and
- (vii) cooperation in Chinese medicine industry.

The two sides agreed on the contents and modalities of cooperation for each of the seven areas above, and that new areas of trade and investment facilitation could be added in future.

FURTHER LIBERALISATION

7. CEPA adopts a building block approach. It provides a mechanism for the inclusion of further market opening and liberalization measures to be agreed between the Mainland and Hong Kong. The Government will continue to pursue requests of the business sectors for further liberalisation on goods and services trade with the Mainland with a view to broadening CEPA's scope and coverage incrementally.