

***Mainland and Hong Kong
Closer Economic
Partnership Arrangement
(CEPA)***

***Preliminary Assessment on
its Economic Impact***

Highlights of CEPA

- The HKSARG and the CPG signed the main parts of CEPA and the six Annexes on 29 June 2003 and 29 September 2003 respectively, which set out the implementation details of CEPA. Key liberalization measures under CEPA came into effect on 1 January 2004.
- CEPA covers three broad areas, namely trade in goods, trade in services (including Individual Visit Scheme (IVS)) and trade and investment facilitation.
- CEPA is top on our trade and economic policy agenda, we would like to understand its impact on Hong Kong's economy in detail.

Scope of Economic Impact Assessment

- At the LegCo C&I Panel Meeting on 10 May 2004, the Administration undertook to conduct a quantitative analysis of the economic impact of CEPA, 9-12 months after CEPA's implementation.
- The study was conducted by CITB, in collaboration with EABFU and C&SD. The study covers three aspects: trade in goods, trade in services, and IVS.
- We would also briefly touch on the trade and investment facilitation measures and its economic impact in the final report.

Progress on Economic Impact Assessment

- At this stage, we have completed the data collection of trade in goods and IVS, and the preliminary analysis.
- The study on trade in services, and the analysis on trade and investment facilitation are in progress.

Notes to Survey Findings

- This study mainly covers the first 9-12 months since CEPA I's implementation.
- The liberalization measures covered in CEPA II which came into effect in 2005 (such as the increased no. of products enjoying zero tariffs from 379 to 1,108, and the further liberalization of trade in services) did not fall within the scope of this study.
- The implementation period of CEPA is still rather short, and the planning of manufacturing, investment and other economic activities takes time. In addition, further liberalization measures of CEPA will continue to be introduced, hence, the present survey results are preliminary, not conclusive. Following the deepening of the effects of CEPA, the economic benefits of CEPA would continue to increase.

Trade in Goods

Trade in Goods – Liberalization

Measures under CEPA in 2004

- The Mainland agreed to eliminate tariffs on imported goods of Hong Kong origin by stages. Hong Kong products under 374 Mainland 2004 product codes (equivalent to 379 Mainland 2005 product codes) meeting CEPA rules of origin could enjoy zero tariff with effect from 1 January 2004.
- These product codes cover some electrical and electronics products, plastic articles, textiles and clothing, chemical products, pharmaceutical products, clocks and watches, jewellery, cosmetics, and metal products, etc.

Trade in Goods – Implementation in 2004

- As at 31 December 2004, TID and the five GACOs received 3,211 CO(CEPA) applications, of which 3,008 applications were approved, involving products with a total value of HK\$1.15 billion.
- According to the data of the Customs General Administration of PRC, 2,577 consignments of products with a total value of HK\$0.99 billion were already imported to the Mainland. The tariff savings amounted to RMB 66 million.

Statistics on CO(CEPA) Applications in 2004

| Product Types | No. of CO(CEPA) Applications Received | No. of CO(CEPA) Applications Approved | Total FOB Value (HK\$) |
|--------------------------------------|---------------------------------------|---------------------------------------|------------------------|
| 1. Textiles and Clothing | 1,300 | 1,193 | 122,417,000 |
| 2. Pharmaceutical Products | 702 | 681 | 737,026,000 |
| 3. Plastics and Plastic Articles | 317 | 308 | 112,335,000 |
| 4. Coloring Matters | 192 | 181 | 52,214,000 |
| 5. Chemical Products | 188 | 170 | 38,687,000 |
| 6. Electrical & Electronic Products | 186 | 183 | 40,048,000 |
| 7. Paper and Printed Articles | 178 | 157 | 10,259,000 |
| 8. Base Metal Products | 66 | 62 | 21,744,000 |
| 9. Jewelry & Precious Metals | 33 | 32 | 3,592,000 |
| 10. Clocks & Watches & Parts Thereof | 29 | 27 | 1,705,000 |
| 11. Others | 20 | 14 | 10,273,000 |
| Total : | 3,211 | 3,008 | 1,150,300,000 |

Monthly Statistics on CO(CEPA) Applications in 2004



Economic Assessment on Trade in Goods - Methodology

- **General Statistical Data**
- **Random Sampling Survey**
 - Questionnaires were sent to over 250 enterprises (30% of them have benefited or intended to be benefited from CEPA, and 70% of them were qualified but yet to be benefited from CEPA) between October and November 2004 by random sampling. Staff were sent to visit some of the enterprises to follow-up. The overall response rate was 75%.
 - The information collected includes: CEPA's impact on Hong Kong's economy, the utilization of CEPA, the investment and employment plans of the enterprises in the past year, and their future business plans, etc.
- **Consultative Interview**
 - Interviewees include manufacturers associations and individual enterprises, to collect their views on how CEPA affect their business prospects and strategies, and the problems encountered when they utilized CEPA.

Trade in Goods – Survey Results

- Overall speaking, respondents are generally positive in respect of CEPA
 - 93% of respondents believe that CEPA is beneficial to the HK economy
 - 89% of respondents consider that CEPA is beneficial to HK's manufacturing sector
 - 53% of respondents indicate that CEPA is beneficial to their company's Mainland-related business

Trade in Goods – Survey Results

- Respondents believe that products with the following features could benefit more from CEPA:
 - High Mainland tariff rate
 - High value-added content
 - High intellectual property right
 - Short product cycle
 - Brand name products
 - Examples: pharmaceutical products, textiles and clothing, plastics and plastic articles, chemical products, and coloring matters.

Trade in Goods – Survey Results

- In the past year, CEPA's impact on the scale of operation of the respondents who have benefited or intended to be benefited from CEPA :
 - 4% of companies increased the area of premises used
 - 6% of companies increased the use of self-owned machinery and equipment
 - 9% of companies increased the no. of staff
- In the next year, CEPA's impact on the scale of operation of the respondents who have benefited or intended to be benefited from CEPA :
 - 5% of companies plan to increase the area of premises used
 - 7% of companies plan to increase the use of machinery and equipment
 - 11% of companies plan to increase the no. of staff

Trade in Goods – Survey Results

■ Looking Forward

➤ 13% of respondents indicate that they will formulate their business plan in the light of CEPA.

Among them,

- 63% indicate that they will extend their business from manufacturing to wholesaling/retailing of goods in the Mainland.
- 28% indicate that they will line up with foreign investors in setting up manufacturing line in Hong Kong.
- 28% indicate that they will increase production/trading of tariff-free goods under CEPA.

Trade in Goods – Impact on HK's Economy

- Specifically, CEPA's impact include:
 - Raise exports through cutting prices via saving tariffs; improve profit margin.
 - Expand local productive capacity through expansion of existing production lines or setting up new production lines.
 - Employment impact should be relatively smaller given the capital-intensive nature of the manufacturing sector of Hong Kong.

CEPA's Impact on HK's Manufacturing Sector

(Relevant Data outside the scope of the Survey)

- As a result of positive external economic factors and CEPA, HK domestic exports to Mainland rebounded significantly:
 - In 2004, HK domestic exports to the Mainland bucking the downtrend in the past 3 years, and recorded a growth of 3.1%.
 - Of which, value of exports of CEPA items to the Mainland stayed roughly the same as last year, bucking the downtrend in the past 3 years.

HK's Domestic Exports in 2004

- Total Domestic Exports: HK\$126 billion
 - Of which, domestic exports to the Mainland: HK\$37.9 billion (30% of total domestic exports)
 - Of which, domestic exports of CEPA I products to Mainland: HK\$24.4 billion (64% of total domestic exports to the Mainland)
 - ❖ Of which, domestic exports to the Mainland which applied for CO(CEPA) to enjoy zero tariff: HK\$1.15 billion (4.7% of total domestic exports of CEPA I products to Mainland)

Response from the Trade

- Overall speaking, the trade's response to trade in goods under CEPA is satisfactory, especially in pharmaceutical products, textiles and clothing, plastic articles, coloring matters, chemical products, and electrical and electronics products.
- Whereas the responses of clocks and watches, food and beverages, leather and furskin articles, etc. were less positive at the moment.

Response from the Trade

- The possible reasons for the lukewarm responses of some products are:
 - Around 70% of HK domestic exports (for textiles and clothing, over 90%) are outward processing trade, mainly for exports, for which import tariff has already been exempted.
 - For certain products, the relevant import tariff may not be a major component in the overall operating cost.
 - Manufacturers applying for CO(CEPA) must registered for Factory Registration (FR), and some manufacturers may not wish to observe the conditions of FR.
 - The business community needs time to plan and adjust to the new system, with a view to entering the Mainland market.
 - The CEPA ROO for about 30% of the product codes are different from the HK ROO, hence some of the manufacturers may not be able to meet the CEPA ROO.
 - Applying for a CO(CEPA) only takes 2 days. Yet for very urgent orders and small value consignments, some manufacturers may forego the tariff preference and aim to complete the transaction as soon as possible.

CEPA's Impact on HK's Manufacturing Sector

(Relevant Data outside the scope of the Survey)

- We understand enterprises need time to familiarize with CEPA; and the coverage of CEPA I is relatively limited, and some new products suitable for the Mainland market are not included, yet we notice that manufacturers are actively expanding their productive capacities, in particular:
 - Investment in machinery and equipment picked up by 18% in real terms in the first 3 quarters of 2004.
 - Factory Registration (excluding textiles and clothing) increased by 5% in 2004.
 - No. of tenants in the industrial estates increased by 3% in 2004.
 - Sales of industrial property became more active.
 - A number of manufacturers expanded their existing local production lines, or set up new ones. For example:
 - Several Chinese herbal medicine enterprises set up operations in the industrial estates to make use of CEPA.

HKSARG's Implementation Efforts

- **HKSARG determines to ensure the smooth implementation of CEPA:**
 - For trade in goods, TID provides one-stop enquiry services, and is one of the CO(CEPA) issuing authorities. To ensure maximum convenience for traders, the application procedures for CO(CEPA) are largely the same as those for the existing CO. Traders could submit their applications through the EDI system. A CO(CEPA) application will normally be approved within 1.5 working days.
 - So far, we have handled over 18,000 enquiries on trade in goods; we also completed the processing of all CO(CEPA) applications within the timeframe of our performance pledge.
 - To facilitate verification of goods at the customs control points and speed up customs clearance, we have also established an electronic data exchange mechanism with the Mainland.

HKARG's Promotion Efforts

- Since the announcement of CEPA, the relevant bureaux/ departments, overseas offices and TDC have been promoting the business opportunities brought about by CEPA to local, Mainland, and foreign investors, with a view to enhancing their understandings on CEPA. These efforts include:
 - Established enquiry telephone hotlines and email service in TID;
 - Established a dedicated CEPA web site in TID, collating and disseminating the relevant updated Mainland laws and regulations, and established hyperlinks with some 120 government web sites in the Mainland to disseminate Mainland rules and regulations more quickly and widely;
 - Introduce the implementation details of CEPA through seminars, exhibitions and other promotional events, and promote CEPA in the Mainland and overseas to attract investment;
 - Step up liaison and cooperation with GD and Shanghai through the HK/GD Cooperation Joint Conference and the HK/Shanghai Economic and Trade Cooperation Conference to attract Mainland enterprises to invest in HK, and to ensure the smooth implementation of CEPA.
- **We would continue with promoting CEPA.**

Individual Visit Scheme (IVS)

IVS – Liberalisation Measures under CEPA

- The Mainland allowed residents of designated areas to visit HK individually for tourism by phase, details as follow:

| Effective Date | Additional Cities/Provinces Covered | Registered population (Mn persons) |
|----------------|--|------------------------------------|
| 28 Jul 2003 | Dongguan, Zhongshan, Jiangmen and Foshan | 10.1 |
| 20 Aug 2003 | Guangzhou, Shenzhen, Zhuhai and Huizhou | 12.2 |
| 1 Sep 2003 | Beijing and Shanghai | 24.7 |
| 1 Jan 2004 | Shantou, Chaozhou, Meizhou, Zhaoqing, Qingyuan and Yunfu | 22.6 |
| 1 May 2004 | All other cities in Guangdong | 31.6 |
| 1 Jul 2004 | Nanjing, Suzhou & Wuxi in Jiangsu; Hangzhou, Ningbo & Taizhou in Zhejiang; Fuzhou, Xiamen & Quanzhou in Fujian | 47.1 |
| | Total: | 148.3 |

Mainland Visitors to HK

| Year/Quarter | Non-IVS Visitors (million) | IVS Visitors (million) | Total Mainland Visitors (million) | % of IVS Visitors |
|--------------|-------------------------------|---------------------------|--------------------------------------|-------------------|
| 2003 Q3 | 2.28 | 0.13 | 2.40 | 5.2% |
| 2003 Q4 | 2.29 | 0.54 | 2.83 | 19.1% |
| 2003 | 7.8 | 0.67 | 8.47 | 7.9% |
| 2004 Q1 | 2.12 | 0.80 | 2.92 | 27.5% |
| 2004 Q2 | 1.95 | 0.80 | 2.75 | 29.1% |
| 2004 Q3 | 1.96 | 1.36 | 3.31 | 40.9% |
| 2003 Q4 | 1.97 | 1.30 | 3.27 | 39.8% |
| 2004 | 7.99 | 4.26 | 12.25 | 34.8% |
| | Total: | 4.93 | | |

Economic Assessment on IVS - Methodology

- Hong Kong Tourism Board interviewed IVS visitors randomly, to estimate the additional trips spurred by IVS and IVS visitors' spending on different items.
- With the net incremental spending on tourism generated by IVS, and applying the results of the econometric model on GDP forecasting, we could estimate the economic impact of IVS on HK's economy.
- Matching the IVS visitors' spending on different items to the related sectors, and making reference to business receipts and the value-added content of the said sectors and their relationship with employment, we could estimate the impact of IVS on major tourism-related industries.

Impact of IVS on HK's Economy

- Following the launch of IVS in July 2003, Mainland residents had made 4.93 million trips to HK under IVS as at end 2004.
- In 2004 alone, Mainland residents had made 4.26 million trips to HK under IVS. Of which, 3.08 million were overnight visitors, the average length of stay was 2.7 nights; the other 1.18 million IVS visitors were same-day visitors.
- Among the visitors visited HK under IVS in 2004, around 2.4 million trips were incremental visits, and the other 1.8 million trips were diversion from other modes of visits to IVS visits.

Impact of IVS on HK's Economy

- Overall speaking, IVS helped rebuild consumer confidence and thereby reviving domestic demand in the HK economy, particularly after the SARS disease. Reflecting at least in part the IVS impact, private consumption expenditure in HK reverted from a fall of 3.7% in the first half of 2003 to a growth of 1.9% in the second half. The growth accelerated further to 7.4% in the first three quarters of 2004.

Assessment in Progress (IVS)

- To assess IVS visitors' spending pattern and the net incremental tourism receipts induced by IVS.
- To assess the impact of IVS on employment.
- To assess the impact of IVS on HK's GDP.
- To assess the impact of IVS on tourism-related industries.

Trade and Investment Facilitation Measures

- We also actively pursue trade and investment facilitation measures:
 - According to the statistics provided by C&SD, as at mid-2004, the no. of Mainland enterprises with regional headquarters and regional offices in HK was 12.9% higher than in the previous year. Out of the 205 investment projects assisted by Invest HK in 2004, 35 were Mainland enterprises, a sharp increase of 106% compared to 17 in 2003.
 - Following MoC's announcement of the new investment facilitation policy in September last year, IHK has put in place a series of measures called "Invest HK One-Stop Service" to provide convenient services for potential Mainland investors who intend to invest in HK. We believe the implementation of CEPA will attract more Mainland enterprises to Hong Kong.

Tasks to be Completed in Q1 2005

- Complete the rest of the analysis on IVS.
- Assess the impact of trade in services under CEPA on HK's economy.
- Evaluate the impact of trade and investment facilitation under CEPA on HK's economy
- Complete the written report on the Economic Impact Assessment.
- Report the comprehensive results of the Economic Impact Assessment on CEPA to the C&I Panel.