

Supplementary information for
meeting on 18 May 2010

Legislative Council
Panel on Commerce and Industry

Relations between the Mainland and Hong Kong
on Industry and Trade Fronts

Introduction

This paper provides supplementary information on the developments relating to industries, trade and technological co-operation between the Mainland and Hong Kong, so as to facilitate discussion on Agenda Item IV “Framework Agreement on Hong Kong/Guangdong Co-operation in relation to trade and industry between the two places” and Item V “Hong Kong/Shenzhen Co-operation Meeting in relation to trade and industry between the two places”.

Trade relations between the Mainland and Hong Kong

2. The Mainland is Hong Kong’s largest trading partner. In 2009, the value of merchandise trade between the Mainland and Hong Kong was HK\$2,512.6 billion, accounting for 48.7% of the total trade value of Hong Kong during the same period. On the other hand, Hong Kong ranks third among the trading partners of the Mainland, after the US and Japan.

3. In terms of investment, Hong Kong is Mainland’s largest source of realised direct foreign investment, accounting for 42.1% of the national total as at the end of March 2010, with a cumulative value of realised direct investment at HK\$3,168.3 billion. At the same time, the Mainland is Hong Kong’s biggest external investor. As at the end of 2008, inward direct investment from the Mainland amounted to HK\$2,311.4 billion, accounting for 36.5% of our total inward direct investment. There are over 2,800 Mainland enterprises in Hong Kong engaging in a wide range of economic activities, including import/export, wholesale/retail, transportation and warehousing.

4. Moreover, Hong Kong has been an important entrepot for the Mainland's merchandise. In 2009, the value of goods re-exported through Hong Kong to the Mainland was HK\$1,236.6 billion, while the value of Mainland goods re-exported through Hong Kong to other parts of the world amounted to HK\$1,503.3 billion.

Business environment faced by Hong Kong enterprises in the Mainland and their concerns

5. Hong Kong businessmen have invested in a large number of manufacturing operations in the Mainland, many of which are in the processing trade. Policies encouraging enterprises to upgrade and restructure and to tap the Mainland domestic market have been incorporated into the Framework Agreement on Hong Kong-Guangdong Co-operation. The two sides will make concerted efforts to ensure the successful implementation of the policies.

6. The HKSAR Government maintains close dialogue with the trade through various channels, including the Task Force to Support the Processing Trade, this Panel, LegCo Members and business associations. The Economic and Trade Offices of the HKSAR Government in the Mainland also maintain close liaison with Hong Kong enterprises in the Mainland.

7. We learnt from the trade that some policies introduced by the Mainland in recent years to facilitate the upgrading and restructuring of enterprises have brought about pressure on their operations. These policies include restricting the operation of polluting, resource-intensive and energy-intensive industries; encouraging enterprises to move up the value-chain, upgrade their production technologies or shift their operation to the central and western regions of the Mainland, etc. In the long run, these policies will benefit the nation's economic development by improving the Mainland's industrial structure and enhancing enterprises' international competitiveness. However, given the shrinking overseas market resulting from the financial turmoil, some of the policies have brought challenges to the operation of Hong Kong enterprises.

8. Although the financial turmoil is subsiding, full recovery of the global economy has yet to be in place. The trade inform us that the profit margins of some enterprises are shrinking due to rising wages, upsurge in the prices of raw materials, the appreciation of renminbi (RMB) and keen competition amidst weak overseas markets which have not fully recovered after the hit of the financial tsunami. In addition, enterprises have encountered difficulties in opening up the Mainland market,

including the lack of Mainland market information, problems in relation to taxation and protection of intellectual properties, etc.

Support measures for Hong Kong enterprises in the Mainland

9. The HKSAR Government maintains close liaison with the relevant Mainland authorities (including the Ministry of Commerce, General Administration of Customs and the Guangdong Province) to convey the trade's views on problems encountered in the process of opening up the Mainland market and in the course of upgrading and restructuring, and to discuss possible support measures for the trade. We have also been appealing to the Mainland to consult the trade and consider their views before promulgating new policies and legislation, and to give the trade sufficient time for transition and adjustment.

Support measures implemented in the Mainland

10. During the financial turmoil, the Mainland authorities responded positively to the proposals of the HKSAR Government and the trade. Various facilitation measures were launched in 2008 and 2009, including raising the export tax rebate rates for a number of times, suspending the actual payment of standing book deposit for processing trade enterprises, reducing or waiving administrative fees and charges, and relieving the burden of social insurance and economic compensation for enterprises with hardship, etc. The Guangdong Province also announced early last year 30 support measures covering nine areas to help Hong Kong, Macao and Taiwan enterprises in the pursuit of restructuring and upgrading. The 30 support measures included the launch of a RMB 1 billion fund for the restructuring and upgrading of processing trade enterprises, reduction or remission of certain taxes and fees, implementation of "restructuring without stopping production" and "consolidated tax return for multiple domestic sales", etc.

11. Since there is still uncertainty over the economic situation this year, we have conveyed to the Mainland authorities the trade's wish for the continued implementation of the support measures launched by the Mainland in 2008 and 2009. The Mainland announced last year that the original expiry date (end of 2009) in respect of measures for alleviating the burden of social insurance and economic compensation for enterprises with hardship would be extended to the end of 2010. This would allow those enterprises affected by the financial crisis to consolidate their business and help stabilise the labour market.

Support measures implemented in Hong Kong

12. Meanwhile, the HKSAR Government provides assistance to enterprises through the SME Funding Schemes in areas such as market promotion, upgrading of operational and technical skills, and securing loans from the commercial market for acquisition of equipment, business restructuring and relocation. As for the Special Loan Guarantee Scheme (SpGS) which was introduced to assist enterprises during the global financial crisis, since the trade may need some time to consolidate their business during the early stage of economic recovery, the HKSAR Government announced on 21 April 2010 that the SpGS would be extended, for the last time, for another six months until 31 December 2010.

13. Regarding the use of design and technology, funding support is provided for Hong Kong enterprises to improve product design and their technological level through the “Innovation and Technology Fund” and the recently launched “Research and Development Cash Rebate Scheme” administered by the Innovation and Technology Commission, and the “Design-Business Collaboration Scheme” run by Create Hong Kong.

14. Furthermore, to assist enterprises in tapping the Mainland market, the HKSAR Government will continue to join hands with the Mainland to organise more business matching forums and trade fairs, and to examine the trade’s proposals to strengthen relevant support measures. Hong Kong traders are encouraged to make good use of trade fairs and matching forums organised by different Mainland provinces and cities to develop new sales channels. The Hong Kong Trade Development Council (HKTDC) organises many trade fairs in the Mainland to enhance the awareness over Hong Kong brand products. Recently organised events include the second “Hong Kong Consumer Products Expo” held in Guangzhou in January and the “Style Hong Kong Show” held in Fuzhou in late April.

15. In addition, the HKTDC publishes useful research materials, such as “Guide to Selling in China” and “Domestic Sales Strategy”, to update Hong Kong traders on the latest developments in the Mainland market. These publications, together with the profiles and statistics of Mainland provinces and cities, have been uploaded onto the HKTDC website for public reference. In April this year, the HKTDC launched a Design Gallery online shop on Taobao, an online trading platform in the Mainland, so that Hong Kong traders can showcase their products directly to Mainland consumers through the internet.

16. Brand building will facilitate enterprises in tapping the Mainland domestic market. In 2009 - 10, the Trade and Industry Department (TID) allocated grants of more than HK\$3.4 million under the SME Development Fund (SDF) to support a number of projects relating to the development and promotion of Hong Kong brands (including the setting-up of showrooms in large-scale exhibitions to showcase Hong Kong products). In addition, the SDF has granted over HK\$1 million to fund surveys and research projects on Mainland domestic sales conducted by a SME support organisation. In December 2009, the TID and HKTDC co-organised a conference entitled “Brand-building - Opening up the Ten Trillion Mainland Domestic Market”, during which entrepreneurs who successfully tapped the Mainland market were invited to share their experience and business insights. Professionals were also invited to speak on topics such as distribution channels in the Mainland, labour laws, customs declaration and taxation, etc. In view of the positive response from participating enterprises, the TID will consider organising similar activities or symposiums in collaboration with the HKTDC and other organisations.

17. The Hong Kong Export Credit Insurance Corporation (ECIC) has launched a series of measures to support the export industry since late 2008. The objective behind these measures (e.g. exercising suitable flexibility in handling SMEs’ application for export credit insurance) is to enable SMEs to continue to develop export trade during the financial tsunami. The ECIC has also extended the measures of offering free buyer credit assessment services and waiving the annual policy fee to the end of September and end of December this year respectively. As regards assisting Hong Kong enterprises in tapping the Mainland market, the ECIC and the China Export and Credit Insurance Corporation signed a Memorandum of Understanding (MOU) in late October 2009. Under the MOU framework, both parties will refer business to each other, hold joint business seminars in Hong Kong and the Mainland and establish regular communication channels.

18. Apart from the above measures, the relevant departments of the HKSAR Government and other support organisations will promote the development of Hong Kong enterprises through the following ongoing efforts:

- (i) organising symposiums and seminars through the TID and Mainland Offices to enhance the trade’s understanding of new policies, legislation and the business environment;
- (ii) disseminating information on Mainland’s trade-related policies, legislation and measures to Hong Kong enterprises through the

websites¹ of the TID and Mainland Offices and by means of circulars and newsletters;

- (iii) organising delegations to visit the Mainland with a view to enhancing the trade's understanding of Mainland policies and market development; and
- (iv) providing Hong Kong enterprises with support services on technological upgrading, improving management, branding and market development, etc. and Mainland market information through support organisations such as the Hong Kong Productivity Council and the HKTDC.

19. As regards depreciation allowances in respect of machinery or plants used in import processing operations, the Legislative Council Panel on Financial Affairs (LegCo FA Panel) had detailed discussions with the Financial Services and the Treasury Bureau (FSTB) at its special meeting held on 14 December 2009. Subsequently, in its letter to the LegCo FA Panel on 10 March 2010, FSTB indicated that the completeness of the anti-avoidance provisions in the Inland Revenue Ordinance (IRO) would be affected if the concerned restriction under the IRO was relaxed. There would also be practical difficulties in implementation opening possible loopholes for abuse. Nevertheless, in response to the trade's request, FSTB has invited the Joint Liaison Committee on Taxation (JLCT) to study the issue. With its members' professional background as well as their knowledge of the tax regime and tax law in Hong Kong, it is hoped that the JLCT can explore at the technical level whether there is any practical and feasible solution to address the concerns of the trade and the Administration. The Administration would consider the JLCT's recommendations carefully once available.

Recent developments in the Mainland and Hong Kong Closer Economic Partnership Arrangement

20. The Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) is a free trade agreement signed between the Mainland and Hong Kong. Since the signing of the main text in 2003, six supplements to CEPA have been signed between the two sides. With the implementation of these liberalisation measures,

¹ The TID's website includes a dedicated page on business information on the Mainland, with hyperlinks to the economic and trade websites of 170 Mainland authorities. This platform facilitates Hong Kong enterprises in getting access to trade-related information on the Mainland.

there are now 1,580 types of goods of Hong Kong origin that can enjoy zero tariff on importation to the Mainland, and Hong Kong service suppliers in 42 service areas can enjoy preferential access to the Mainland market.

21. As at 30 April 2010, more than 54,000 Certificate of Origin applications under CEPA have been approved, with a total export value of goods amounting to over HK\$23.5 billion. Major categories of goods include pharmaceutical products, plastics and plastics articles, textiles and clothing, and food and beverages. As for trade in services, over 2,200 Hong Kong Service Supplier Certificates have been issued to over 1,200 Hong Kong enterprises, mostly in the transportation and logistics, distribution, air transport and advertising sectors.

22. We will continue to maintain close co-operation with the Mainland authorities to ensure effective implementation of CEPA measures. The HKSAR Government has commenced consultations with the Mainland authorities on further liberalization measures since early this year. We will announce the outcome upon conclusion of the discussions.

Hong Kong/Guangdong and Hong Kong/Shenzhen technology co-operation

23. The Framework Agreement on Hong Kong/Guangdong Co-operation has reaffirmed that Guangdong and Hong Kong should capitalise on their own advantages to jointly and strategically develop innovation and technology. Specifically, Governments of the two places have been sponsoring collaboration on research and development (R&D) platforms between the two places in selected technology areas through the annual “Guangdong-Hong Kong Technology Co-operation Funding Scheme” (GD-HK TCFS). Since 2004, Hong Kong and Guangdong have jointly supported over 30 R&D projects with total funding of around \$200 million. The GD-HK TCFS this year is expected to be launched in mid 2010.

24. In addition, the Framework Agreement on Hong Kong/Guangdong Co-operation has also reaffirmed the positioning of the “Shenzhen/Hong Kong Innovation Circle” set up in 2007. With a view to further promoting the development of the “Shenzhen/Hong Kong Innovation Circle”, the Steering Group on Shenzhen/Hong Kong Co-operation in Innovation and Technology approved a “Three-year Action Plan” at its third meeting held in March 2009. The Action Plan, which seeks to deepen technological co-operation between the two places, contains 24 collaboration projects in various fields, including biomedical, integrated circuit, RFID technology, solar energy and industrial design. Co-operation partners comprise government

departments, universities, R&D institutions and community organisations of both places.

25. Co-operation in information and communication technology between Hong Kong and Guangdong is mainly conducted through the Expert Group on Co-operation in Informatisation (EGCI), which is established under the aegis of the Hong Kong/Guangdong Co-operation Joint Conference. "The Application Procedure for Pilot Project on Mutual Recognition of Electronic Signature Certificates Issued by Hong Kong and Guangdong" was announced on 15 April 2010 to facilitate the adoption of electronic signature certificates for cross-border services. Recognised Certification Authorities in Guangdong and Hong Kong and their partners may submit applications. This will be implemented as a pilot measure in Guangdong.

Conclusion

26. We will continue to communicate with the trade and keep a close watch over the business environment and development of the trade. In order to facilitate the further development of Hong Kong enterprises, we will follow up on the trade's proposals on business facilitation and explore opportunities for cooperation with the Mainland pursuant to the policy direction of the Framework Agreement on Hong Kong/Guangdong Co-operation.

Commerce and Economic Development Bureau
May 2010