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Panel on Commerce and Industry
Panel on Economic Development
Panel on Financial Affairs

Minutes of joint meeting
held on Friday, 20 July 2018, at 4:30 pm
in Conference Room 1 of the Legislative Council Complex

Members present : Members of the Panel on Commerce and Industry

- *# Hon WU Chi-wai, MH (Chairman of the Panel on
Commerce and Industry)
- *# Hon SHIU Ka-fai (Deputy Chairman)
- *# Hon WONG Ting-kwong, GBS, JP
- * Hon YIU Si-wing, BBS
Hon MA Fung-kwok, SBS, JP
- *# Hon Charles Peter MOK, JP
Hon CHAN Chi-chuen
- * Hon Martin LIAO Cheung-kong, SBS, JP
Dr Hon CHIANG Lai-wan, SBS, JP
- *# Ir Dr Hon LO Wai-kwok, SBS, MH, JP
- *# Hon CHU Hoi-dick

Members of the Panel on Economic Development

- # Hon Alvin YEUNG (Deputy Chairman)
- # Hon James TO Kun-sun
- # Hon Paul TSE Wai-chun, JP
Hon Claudia MO
Hon Steven HO Chun-yin, BBS
Hon Frankie YICK Chi-ming, SBS, JP
Dr Hon Elizabeth QUAT, BBS, JP
- # Hon Holden CHOW Ho-ding
- # Hon LUK Chung-hung, JP
Hon Jeremy TAM Man-ho

Members of the Panel on Financial Affairs

- * Hon Kenneth LEUNG (Chairman of the Panel on Financial Affairs)
- Hon CHEUNG Kwok-kwan, JP

Members absent : Members of the Panel on Commerce and Industry

- # Hon Mrs Regina IP LAU Suk-ye, GBS, JP
- *# Hon Dennis KWOK Wing-hang
- * Hon CHUNG Kwok-pan
- * Hon Jimmy NG Wing-ka, JP
- *# Hon CHAN Chun-ying, JP
- Hon Tanya CHAN
- Hon LAU Kwok-fan, MH

Members of the Panel on Economic Development

- ^# Hon Jeffrey LAM Kin-fung, GBS, JP (Chairman of the Panel on Economic Development)
- # Hon Starry LEE Wai-king, SBS, JP
- Hon WONG Kwok-kin, SBS, JP
- Hon Michael TIEN Puk-sun, BBS, JP
- Hon Alice MAK Mei-kuen, BBS, JP
- Hon Andrew WAN Siu-kin
- # Dr Hon Junius HO Kwan-yiu, JP

Members of the Panel on Financial Affairs

- ^* Hon Christopher CHEUNG Wah-fung, SBS, JP (Deputy Chairman)
- Hon Abraham SHEK Lai-him, GBS, JP
- Hon CHAN Kin-por, GBS, JP

- ^ Also members of the Panel on Commerce and Industry
- * Also members of the Panel on Economic Development
- # Also members of the Panel on Financial Affairs

Member attending : Hon AU Nok-hin

**Public officers
attending**

: Agenda item II

Mr Paul CHAN Mo-po, GBM, GBS, MH, JP
The Financial Secretary

Mr James Henry LAU Jr, JP
Secretary for Financial Services and the Treasury

Mr Edward YAU Tang-wah, GBS, JP
Secretary for Commerce and Economic Development

Ms Salina YAN, JP
Director-General of Trade and Industry

Mr Andrew AU, JP
Government Economist

Mr Willy TSOI
Administrative Assistant to the Financial Secretary

Clerk in attendance : Mr Desmond LAM
Chief Council Secretary (1)3

Staff in attendance : Ms Connie HO
Senior Council Secretary (1)3

Mr Joey LO
Senior Council Secretary (1)8

Mr Terence LAM
Council Secretary (1)3

Ms May LEUNG
Legislative Assistant (1)3

Miss Zoe YIP
Clerical Assistant (1)3

I. Election of Chairman

Mr Kenneth LEUNG, Chairman of the Panel on Financial Affairs, informed members that Mr WU Chi-wai, Chairman of the Panel on Commerce and Industry and Mr Jeffrey LAM, Chairman of the Panel on Economic Development had agreed that the joint meeting be chaired by him. In accordance with rule 22(k) of the House Rules, members agreed that Mr LEUNG should chair the joint meeting.

II. The impact of trade conflict between China and the United States on Hong Kong's economy

(LC Paper No. CB(1)1268/17-18(01) -- Administration's paper on "The Impact of the Trade Conflict between China and the United States on Hong Kong's Economy"

LC Paper No. IN14/17-18 -- Paper on "Trade conflict between China and the United States and its impact on Hong Kong's economy" prepared by the Research Office of the Legislative Council Secretariat (information note))

Presentation by the Administration

2. At the invitation of the Chairman, The Financial Secretary ("FS") briefed members on the major developments of the trade conflict between the United States ("US") and the Mainland, and the Government's assessment on the economic impact on Hong Kong and follow-up actions in respect of the latest circumstances. Details were set out in the Administration's paper (LC Paper No. CB(1)1268/17-18(01)).

Discussion

Maintaining banking system stability

3. Ms Claudia MO sought details of the measures which the Administration would put in place to strengthen banking system resilience to the adversity that might be experienced in the trade conflict between the US and the Mainland on Hong Kong's economy. FS advised that banks of Hong Kong were under prudential supervision of the Hong Kong Monetary Authority ("HKMA") and had been performing well. Currently, the local banking system had an overall liquidity coverage ratio of around 150% and capital adequacy ratio of over 19%, which stood among the highest in the world. Besides, the non-performing loan ratio was just about 0.6%, showing that the overall asset quality remained at a healthy level.

HKMA would regularly conduct on-site and thematic supervisory reviews and stress tests on banks to ensure that the banking system had sufficient capital and liquid assets to weather shocks. Hong Kong's more than US\$430 billion worth of foreign exchange reserves also provided a powerful line of defence for Hong Kong's monetary and financial stability. The Administration and HKMA would continue to exercise prudential supervision of banks and closely monitor their businesses to ensure stability of the banking system.

4. In view of the latest developments of the US-China trade conflict and in order to reduce the US' influence on Hong Kong's economy, Mr LUK Chung-hung enquired whether the Administration would consider making changes to the Linked Exchange Rate System ("LERS") by removing its currency peg to the US dollar and linking to a basket of currencies. ES responded that LERS had been operating effectively in serving Hong Kong's economy since its implementation in 1983, and stressed the Government's determination to maintain LERS.

Diversification of economy

5. Mr Charles Peter MOK opined that the Administration should be better prepared to turn the threats and crises which might be raised by the trade conflict between the US and the Mainland into opportunity for Hong Kong by stepping up the Government's efforts on promotion of inward investment, in particular investment in the areas of innovation and technology ("I&T"), with a view to alleviating the impact of the trade conflict on Hong Kong's traditional goods trade and fostering the development of new economic activities in Hong Kong. Mr MOK advised that Hong Kong's traditional role as the buffer between the Mainland and other countries, in particular the US, and Hong Kong's advantages under "One Country, Two Systems", which made Hong Kong distinct from other Mainland cities, should be widely promoted to the international community in its inward investment promotion work.

6. Mr WU Chi-wai concurred with Mr Charles Peter MOK's view and considered that the Administration should be more proactive in attracting inward investment in the face of keen competition from Singapore, which offered tailor-made arrangements for individual target companies. Mr WU opined that the Administration should, apart from the policy initiatives set out in the Chief Executive's 2017 Policy Address ("2017 Policy Address"), consider putting in place more robust policy measures, such as preferential policies in terms of land and taxation, to attract multinational companies of I&T industry to set up research and development ("R&D") centres in Hong Kong, thereby expediting the diversification of Hong Kong's economy.

7. ES responded that under the unique arrangement of "One Country, Two Systems", Hong Kong's strengths lied in its common law jurisdiction, robust legal

system, free flow of capital, goods, information and talent, and sound intellectual property protection regime. FS agreed that I&T would be a key driver for Hong Kong's future economic development and a major source of quality employment opportunities for young people. The Administration had mapped out in the 2017 Policy Address and the 2018-2019 Budget a master plan in respect of I&T development to promote diversification of Hong Kong's economy. In gist, the Administration would focus on four technology areas where Hong Kong possessed advantages and strived to develop, namely, biotechnology, artificial intelligence ("AI"), smart city and financial technologies. The major policy initiatives included, among others, the establishment of two research clusters, healthcare technologies and AI and robotics technologies, to attract the world's top scientific research institutions and technology enterprises to Hong Kong for conducting more midstream and downstream R&D projects in collaboration with local universities and scientific research institutions, and the setting up of the Data Technology Hub and the Advanced Manufacturing Centre at the Tseung Kwan O Industrial Estate in 2020 and 2022 respectively to promote re-industrialization.

8. FS added that with a view to encouraging private enterprises to increase investment in R&D, the Administration would introduce enhanced tax deduction for domestic expenditure on R&D where enterprises could enjoy a 300% tax deduction for the first HK\$2 million qualifying R&D expenditure, and a 200% deduction for the remainder. FS reiterated that the Administration would adhere to the above master plan and provide the necessary resources to promote the long-term development of I&T in Hong Kong. That said, the Administration would continue to roll out special measures to support small and medium enterprises ("SMEs") as and when necessary to tide over their difficulties in the face of the US-China trade conflict.

9. In respect of inward investment promotion, FS advised that Invest Hong Kong ("InvestHK"), the Hong Kong Trade Development Council ("HKTDC") and the overseas Economic and Trade Offices ("ETOs") were tasked to promote trade and investment in different aspects. InvestHK maintained close ties with the overseas offices of HKTDC and ETOs to identify targets and proactively attract overseas enterprises to Hong Kong. Meanwhile, the Administration would seek to better coordinate the work of the three parties with policy steer from the Chief Executive to enhance their overall effectiveness. FS added that playing the dual role of a "facilitator" and a "promoter", the Administration would review regulatory and tax requirements to remove red tape and create a business-friendly environment. In this connection, the Administration would implement relevant tax concessionary measures, and leverage on the Belt and Road Initiative and the Guangdong-Hong Kong-Macao Greater Bay Area ("Bay Area") development to promote Hong Kong as a platform for financing Belt and Road projects as well as accessing the vast market of the Bay Area. FS assured members that the Administration would continue to strengthen investment promotion by leveraging on Hong Kong's advantages under

the "One Country, Two Systems" to foster the sustainable development of Hong Kong's economy.

Support measures to small and medium enterprises

10. In the face of the challenges arising from the US-China trade conflict, Mr Holden CHOW remarked that SMEs were most concerned about the liquidity issue in the short term. He enquired whether the Administration would consider further extending the special concessionary measures under the SME Financing Guarantee Scheme ("SFGS") beyond February 2019 and enhancing the maximum amount of loan guarantee to SMEs under the SME Loan Guarantee Scheme to assist SMEs in securing loans from banks to tide over their financing and liquidity difficulties. Pointing out that Hong Kong exporters might be affected by the possible cuts in export orders amidst the trade conflict between the two countries, Ir Dr LO Wai-kwok urged the Administration to enhance support measures for exporters in terms of export credit insurance.

11. FS advised that the Administration had put in place a number of measures to assist SMEs in responding to the changes in business environment and their operational needs in the face of the trade tension between the US and the Mainland. Where necessary, the Administration was committed to further extending the special concessionary measures and enhancing the maximum amount of loan guarantee under SFGS to assist enterprises in tiding over their liquidity needs. HKMA also reminded banks to render support for SMEs to tackle their financing needs to the extent permitted under their credit policies and risk management principles. In addition, the Hong Kong Export Credit Insurance Corporation introduced in June 2018 special enhanced measures to strengthen protection for Hong Kong exporters with a view to alleviating the rising credit risks arising from the US-China trade conflict.

12. Ir Dr LO Wai-kwok advised that the Administration should maintain close liaison with the trade in respect of the latest developments of the trade conflict between the US and the Mainland, so that the trade could take appropriate actions, such as attending relevant hearings held by the US Government and submitting applications for exemption under the relevant tariff measures, in a timely manner. Dr Elizabeth QUAT urged the Administration to implement targeted measures to assist industries affected by the trade conflict in exploring new markets, and to consider ways to enhance the awareness of SMEs on the economic impact of the trade conflict and to get themselves prepared for the challenges ahead. Mr LUK Chung-hung called on the Administration to vigorously promote diversification of industries and explore new markets to reduce Hong Kong's reliance on the US market. FS said that the Secretary for Commerce and Economic Development ("SCED") had met with local chambers of commerce and maintained

close communication with them to keep them abreast of the latest developments and to better understand the concerns and needs of SMEs.

13. SCED advised that the Administration considered it pivotal to engage the trade in working out the directions to respond to the impact brought by the trade conflict between the US and the Mainland. To enable the trade to accurately grasp the latest situation and understand their concerns, he, together with representatives of the Commerce and Economic Development Bureau ("CEDB") and the Trade and Industry Department ("TID"), had already held five meetings with major local chambers of commerce and SME associations since February 2018. CEDB had also followed up the issues and concerns of the trade raised at the meetings and liaised with the relevant ETOs for relevant information and responses. In addition, HKTDC would organize free seminars with experts helping the trade understand the relevant trade measures and possible responses.

14. SCED added that on the tariff measures arising from the report of the "Section 232 investigation" which had a direct impact on Hong Kong's products, the Administration had provided advice and assistance to manufacturers who intended to make representation to the US Department of Commerce to exclude their products from the tariffs. In addition, the Administration had, through the American Chamber of Commerce in Hong Kong, reflected to the US Government the common interest of Hong Kong and American companies operating here. SCED reiterated that the Administration would continue to keep the trade informed of the latest developments of the US-China trade conflict in a timely manner through commercial information circulars and other channels, and liaise closely with the trade. In this regard, TID had set up a one-stop help desk for better communication with and dissemination of information to the trade.

15. In respect of exploring new markets, ES advised that Hong Kong had entered into a Free Trade Agreement ("FTA") with the Association of Southeast Asian Nations ("ASEAN") in November 2017. In addition to the two ETOs in Singapore and Indonesia, the Administration planned to set up another ETO in Thailand to further enhance the economic and trade ties between Hong Kong and ASEAN. The Administration would also advance the launch of the ASEAN Programme under the Dedicated Fund on Branding, Upgrading and Domestic Sales to August 2018 to provide funding support to individual non-listed Hong Kong enterprises to undertake projects for enhancing their competitiveness and furthering business development in the ASEAN markets with the funding ceiling per project being HK\$1 million. Meanwhile, HKTDC would step up efforts to help the trade develop emerging markets and transfer production base through organizing trade missions and business matching services, etc.

16. In response to some members' views of reducing Hong Kong's reliance on the US market, SCED advised that the US, which was the second largest merchandise

trading partner of Hong Kong 20 years ago, was now at the fourth place. ASEAN had overtaken the US and become Hong Kong's second largest merchandise trading partner. In the past 12 months, Hong Kong had entered into FTAs with more than 12 countries and places. The Administration would continue to forge FTAs and investment promotion and protection agreements with more trading partners in the future.

17. The Chairman enquired about the strategic role of the Bay Area development to Hong Kong in the context of the trade conflict between the US and the Mainland. FS advised that the Bay Area development was a national development strategy seeking to achieve greater economic synergy in the region. Linking nine Guangdong cities, together with Macao and Hong Kong, the Bay Area hosted a combined population of about 68 to 69 million and a collective GDP worth about US\$1.5 trillion, which was comparable to that of Australia or Korea. Hong Kong could take full advantage of the significant opportunities under the Bay Area development and the Belt and Road Initiative to explore new markets and drive economic growth.

Impact on Hong Kong's export trade and inbound tourism

18. Dr CHIANG Lai-wan sought details of the impact of the US' tariff measures on Hong Kong's economy, in particular on the export trade. FS advised that in respect of the tariff measures of an additional 25% tariff imposed on a list of Mainland goods worth US\$50 billion ("the first list"), which arose from the "Section 301 investigation" report, about HK\$53 billion of the concerned Mainland products were re-exported via Hong Kong to the US in 2017, accounting for 19% of all Mainland goods re-exported via Hong Kong to the US, and 1.4% of Hong Kong's total exports of goods. Taking into account other relevant trade and economic activities which supported the US-China trade involving Hong Kong, the impact of the above US' tariff measures on Hong Kong's economic growth this year would be a drag of around 0.1-0.2 percentage point.

19. SCED supplemented that the latest tariff list of 6 031 Mainland items worth US\$200 billion, on which an additional 10% tariffs would be imposed as announced by the US on 10 July 2018, involved a much broader merchandise trade flows through Hong Kong. If the latest tariff list was fully implemented and taken together with the first list, HK\$136.5 billion worth of Mainland goods would be affected, accounting for 49% of Mainland products re-exported via Hong Kong to the US and 3.5% of Hong Kong's total exports of goods basing on Hong Kong's total exports of goods in 2017. FS added that depending on whether and when the latest tariff list would be implemented, it was expected that the direct impact of the tariff measures on Hong Kong's economic growth would emerge later this year and next year while the relevant indirect impact remained to be seen.

20. Mr YIU Si-wing expressed concern about the impact of the escalating trade tension between the US and the Mainland and the recent depreciation of Renminbi ("RMB") on inbound tourism of Hong Kong. Mr YIU considered that the Administration should leverage on the tourism opportunities of the Bay Area development and step up collaboration with the relevant Mainland authorities to develop new tourism products and tourism promotion in South East Asia countries, which were less affected by the US-China trade conflict.

21. FS explained that the depreciation of RMB in recent months largely reflected the strengthening of US dollar. In fact, the extent of depreciation of RMB against US dollar was broadly the same as that of the appreciation of the US dollar against a basket of other major currencies during the past few months and there was no sign of increasing speculative activities in relation to the depreciation of RMB. He said that as reiterated by the People's Bank of China, China would maintain the RMB exchange rate basically stable at a reasonable and balanced level, and RMB depreciation would not be adopted as a means to counter US' tariff measures.

22. SCED said that the US-China trade conflict might affect international trade and world's economic growth, thus having a negative impact on consumers' income. In respect of promotion of tourism development, the Administration would implement the four development strategies as set out in the Development Blueprint for Hong Kong's Tourism Industry released by the Tourism Commission in 2017. The major work included, among others, attracting medium- to long-haul and high consumption visitors, and promotion of MICE (i.e. Meetings, Incentives, Conventions and Exhibitions) travel. SCED added that development of the Bay Area and the completion of several major infrastructure projects would bring in more tourists for Hong Kong and provide opportunity for the development of more multi-destination itineraries and products featuring Hong Kong. In this connection, a tourism forum under the themes of the Belt and Road and the Bay Area would be organized.

Liaison work and strategy

23. Mr AU Nok-hin pointed out that according to the US-Hong Kong Policy Act enacted by the US Congress in 1992, the US Government should continue to treat Hong Kong as a territory which was different from the Mainland in terms of political, economic and trade policies. He advised that the Administration should leverage on the special status of Hong Kong under the US-Hong Kong Policy Act in its negotiations with the US to exclude Hong Kong from the tariff measures arising from the report of "Section 232 investigation" regarding steel and aluminium products. He also suggested that the Administration should identify room for cooperation between the US and Hong Kong to persuade the US Government to return to the negotiation table.

24. SCED responded that pursuant to Article 116 of the Basic Law ("BL"), Hong Kong was a separate custom territory and could participate in the World Trade Organization ("WTO") under the name "Hong Kong, China". Hence, Hong Kong's position at WTO was on par with that of the US. Given that the US-Hong Kong Policy Act was a piece of US' domestic legislation, the Administration considered it more appropriate to pursue with the US side on excluding Hong Kong from the tariff measures arising from the "Section 232 investigation" report, which was considered discriminatory and unfounded, by leveraging on the special status conferred upon Hong Kong under the relevant provisions of BL through bi-lateral negotiations and the WTO platform. SCED further said that there was much room for cooperation between the US and Hong Kong in other areas, such as professional services and investment, apart from trade in goods. Given that US' tariff measures would also prejudice the interest of some local companies in the US, the Administration would lobby for support from the relevant sectors in the US in respect of Hong Kong's position.

25. Mr Alvin YEUNG noted that SCED would visit the US in September 2018. Pointing out that US' tariff measures arising from the reports of "Section 232 investigation" and "Section 301 investigation" had direct and indirect impact on Hong Kong respectively, Mr YEUNG suggested that government officials of a higher level, such as FS, should represent the Hong Kong Government to visit the US to sound out to the US Government the stance and position of the Hong Kong in respect of the relevant tariff measures and to lobby for support from policy-makers, politicians, members of the Congress and the business community of the US on Hong Kong's position. In Mr YEUNG's view, the relevant stakeholders in the US should be reminded of Hong Kong's special status under the US-Hong Kong Policy Act and the fact that Hong Kong was not just one of the Mainland's cities but a separate custom territory under BL. Mr LUK Chung-hung enquired about the measures to be adopted by the Hong Kong Government to counter the US' tariff measures.

26. SCED responded that high-level visits by senior government officials to Hong Kong's major trading partners, including the US, was an on-going initiative of the Administration in strengthening the trade relations between Hong Kong and the relevant economies. Liaison work was also carried out on an on-going basis with the Government's interlocutors in the US, including members of the Congress, think tanks and chambers of commerce, on major policies of the US Government having an impact on Hong Kong. SCED stressed that the current position of the US Government on the tariff issue should not affect the long-term and close trade relations between Hong Kong and the US.

27. On tariff measures in respect of steel and aluminium products arising from the "Section 232 investigation" report, SCED said that the Administration had repeatedly reiterated to the US Government Hong Kong's position and request to exclude Hong Kong from such measures through bilateral negotiations and the WTO

platform. The Administration had also made formal requests to join as third party in the consultations requested by the Mainland, India and the European Union respectively with the US under the WTO Dispute Settlement Mechanism in order to safeguard Hong Kong's interests. However, the relevant requests had been turned down by the US and the Administration was considering the next step. The Administration did not preclude the possibility of making a direct request for consultations with the US.

28. FS noted Mr Alvin YEUNG's suggestion and said that following SCED's visit to the US in September 2018, the Administration would consider how best to deal with the situation having regard to the latest developments of the negotiations with the US side. FS reiterated that as the US-China trade conflict was expected to last for a rather long period of time, the Administration would enhance management of financial risks and take necessary measures to maintain Hong Kong's financial stability, and provide necessary support to local enterprises to tide over their difficulties.

29. The Chairman enquired about the message that would be put across by the Government to the US Government and relevant sectors of the US community during the forthcoming SCED's visit to the US. SCED reiterated the Government's position that trade barriers of any form would benefit no one but result in a lose-lose situation. Citing the examples of reduction of wine tax which eventually turned Hong Kong into a major international wine trading hub and the recent proposal of reduction of profits tax put forth by the Government, SCED said that eliminating trade barriers would benefit all investors in Hong Kong irrespective of which countries they were from since Hong Kong provided a level playing field for all businesses. Should the multilateral trading system under the WTO platform fail to be upheld, international trade would become even more chaotic and the interest of various economies would be prejudiced as a result.

Expanding the network of overseas Economic and Trade Offices

30. Considering that the establishment of the overseas ETOs in the US was relatively small compared with similar set-ups of Singapore and Taiwan, the major competitors of Hong Kong in the region, Mr Alvin YEUNG and Mr Jeremy TAM Man-ho shared the same view that the Administration should consider strengthening the manpower of the existing ETOs in the US and setting up more ETOs in the country. Mr TAM also suggested that the Administration should consider expanding the ETO network to cover countries in Africa and South America so as to explore new trade partners to avoid Hong Kong's over-reliance on certain markets.

31. SCED responded that the Administration had allocated a significant amount of resources for the operation of the ETOs in the US. Of the existing 12 overseas ETOs, three were located in the US, namely Washington DC, New York and San

Francisco. While the manpower provision of the three ETOs might not be comparable to that of similar establishments of other economies having diplomatic-related set-ups in the US, the three ETOs had performed their role effectively in presenting Hong Kong's trade and economic interests in the US and promoting bilateral cooperation between the two places. In particular, the ETOs were successful in engaging a wide spectrum of interlocutors who could exert influence on the US Government, members of the Congress, think tanks and relevant sectors on matters of interest to Hong Kong.

32. In respect of the proposal of expanding the ETO network, SCED explained that in selecting places for setting up new ETOs, the Administration had taken into account a number of factors, including the countries' trade relations with Hong Kong, their economic development potentials, and whether there was scope for Hong Kong to enhance its presence in the regions around the countries. Further expansion of the ETO network would be guided by the above considerations as well as the development of the Belt and Road Initiative.

III. Any other business

33. There being no other business, the meeting ended at 6:25 pm.