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## INFORMATION NOTE

### Economic and trade ties between Hong Kong and Taiwan

#### 1. Introduction

1.1 This information note provides the Panel on Commerce and Industry with information on the ties between Hong Kong and Taiwan in the aspects of trade, investment, tourism and the stock market, as well as the impact of the "Three Direct Links"<sup>1</sup> policy on the Hong Kong economy and the economic stimulus measures of Taiwan.

#### 2. Basic information about Taiwan

2.1 Taiwan has an area of approximately 36 000 km<sup>2</sup>, with a population of some 23 million as at the end of 2008. In 2007, its gross domestic product (GDP) was US\$390.9 billion (HK\$3,043.9 billion)<sup>2</sup>, or a GDP per capita of US\$17,124 (HK\$133,345<sup>3</sup>). Its major economic sectors are electronic products, semiconductors, biotechnology and tropical agricultural products. The Taiwan authority has also reinforced its commitment in furthering the development of nanotechnology and optoelectronics<sup>4</sup> as well as actively promoting its tourism industry.

#### Recent economic situation of Taiwan

2.2 Hard hit by the global financial tsunami, the Taiwan economy experienced a sharp downturn in 2008. The economic growth rate was a mere 0.12%, which was far below the 2007 figure of 5.7%. As the impact of the financial tsunami has yet to recede and the global business environment continues to deteriorate, the economic forecast for 2009 even projects a negative growth of 2.97%. Taiwan's unemployment rate also continues to climb up, reaching a six-year record high of 5.31% in January 2009.

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<sup>1</sup> They are direct links in transportation, trade and postal services.

<sup>2</sup> The average exchange rate in 2008 was US\$1=HK\$7.787.

<sup>3</sup> This represents roughly 57% of Hong Kong's comparable figure.

<sup>4</sup> Optoelectronics is based on the quantum mechanical effects of light on semiconducting materials, products of which include solar cells, photo diodes, photo transistors, photo multipliers, photo resistors and photo conductive camera tubes.

2.3 Taiwan's external trade also fell victim to the sluggish global economy and experienced a slowdown. The trade surplus in 2008 was US\$14.9 billion (HK\$116 billion), down 45.9% from 2007. The export value in 2008 increased slightly to US\$255.7 billion (HK\$1,991.1 billion), up 3.6% from the previous year. Major exports comprised electronic products, metal products, precision instruments and rubber products. In comparison to 2007, import value in 2008 rose to US\$240.8 billion (HK\$1,875.1 billion), mostly driven by an increase in oil import.

### **3. Economic and trade ties between Hong Kong and Taiwan**

#### Trade

3.1 Taiwan was the fifth largest trading partner of Hong Kong in 2008, with the total trade valued at HK\$247 billion, accounting for 4.2% of Hong Kong's overall trade value. Taiwan was also the sixth largest export market of Hong Kong. The overall export value from Hong Kong to Taiwan amounted to HK\$54.9 billion. These figures reflect the close trade ties between Hong Kong and Taiwan.

#### Investment

3.2 Taiwan is a major source of inward direct investment (IDI) in Hong Kong. As at the end of 2007, Taiwan was the tenth major source of IDI in Hong Kong with an IDI stock of HK\$39.9 billion. In June 2008, there were 26 regional headquarters, 158 regional offices and 149 offices in Hong Kong representing Taiwan companies. Furthermore, over 5 000 Taiwan companies established their presence in Hong Kong to support their Taiwan parent companies in performing functions such as corporate management, fund transfers, purchasing and marketing.

#### Tourism

3.3 In 2008, there were over 2.24 million visitor arrivals from Taiwan, accounting for 7.6% of the total visitor arrivals in Hong Kong. At the same time, the number of Hong Kong visitors to Taiwan exceeded 300 000. These figures indicate frequent movement of travellers between the two places. With effect from 1 January 2009, the Hong Kong Government has introduced two new measures to facilitate visits from Taiwan to Hong Kong, namely lifting the restriction that only two iPermits can be applied within 30 days and extending the period of stay in Hong Kong from 14 days to 30 days for holders of iPermits and multiple entry permits.

### Stock market

3.4 Currently, over 50 Taiwan companies are listed in Hong Kong's stock market, including renowned companies such as Foxconn International, Tingyi, TPV Technology, Proview International, Want Want China and Uni-President.

## **4. Impact of the "Three Direct Links" policy on the Hong Kong economy**

4.1 The Mainland and Taiwan authorities agreed in early November 2008 to implement the "Three Direct Links" policy which included direct air, maritime and postal links across the Taiwan Strait. The policy was officially launched on 15 December 2008<sup>5</sup>.

4.2 As the "Three Direct Links" policy has only been implemented for a very short period of time, the Hong Kong Government, experts, academics and industry practitioners are yet to provide data analyses to quantify any substantive economic impact of the policy on the Mainland, Hong Kong and Taiwan. According to available research studies, there are diverging views in the preliminary assessments of the impact of the "Three Direct Links" policy on the Hong Kong economy.

### Views of the Hong Kong Government

4.3 In its preliminary assessment published in November 2008, the Hong Kong Government estimated that the number of Taiwan travellers going to and from the Mainland through the Hong Kong International Airport (HKIA) would be affected to a larger extent. Besides, the "Three Direct Links" policy would also impact on the volume of transshipment cargo as such cargo simply had airside transfer at the HKIA without involving other logistics processes.

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<sup>5</sup> The Mainland and Taiwan authorities signed four agreements in November 2008, including the Cross-Strait Air Transport Agreement and the Cross-Strait Sea Transport Agreement. The main specific provisions include: the number of cross-strait chartered passenger flights has increased from 36 to 108 every week, which can be operated throughout the week instead of on weekends as in the past, and the number of flight points on the Mainland has increased from five cities to 21 cities. There are 60 cross-strait chartered cargo flights per month, with two flight points on the Mainland and two flight points in Taiwan. Each side may add another 15 flights during the peak season from October to November. As for sea transport, the Mainland has opened 63 ports and Taiwan has opened 11 ports. Yet the agreement is only applicable to vessels of Mainland/Taiwan capital which are registered in Hong Kong.

4.4 As for sea freight, 604 000 TEUs of transshipment cargo from the Mainland and Taiwan were shipped to and from the Pearl River Delta (PRD) region via Hong Kong in 2007, representing 3% of the total laden container throughput of Hong Kong. Therefore, the Hong Kong Government estimated that with Hong Kong's cost and geographic advantages, the "Three Direct Links" policy would have relatively less impact on its role in transshipment for PRD ports. In 2007, transshipment from the two sides via Hong Kong to and from ports outside PRD totalled 138 000 TEUs, representing 0.7% of Hong Kong's total laden container throughput. Under the "Three Direct Links" agreement, although quite a number of ports on both sides were opened, the vessels permitted to operate must be of Mainland/Taiwan capital and were registered in Hong Kong. While the development affected Hong Kong's role as a transshipment port, it should be on the whole beneficial to container and bulk cargo shipping operators. It also had positive impacts on local maritime services such as shipping registration and ship insurance businesses.

4.5 In respect of tourism, cross-strait direct flight was conducive to the development of business and leisure travels in the region. This might be favourable to the tourism industry in Hong Kong but the number of Taiwan same-day transit travellers through Hong Kong would decrease.

#### Views of the Hong Kong Trade Development Council

4.6 The Hong Kong Trade Development Council<sup>6</sup> (HKTDC) shares similar views with the Hong Kong Government. According to the research report entitled "'The Three Links': Delivering the Ties of Synergy" published by HKTDC in June 2008, the "Three Direct Links" policy was expected to bring increasing business flows across the Strait and better division of labour in the region. However, the "Three Direct Links" policy would create a greater impact on passengers using Hong Kong as a transit for travelling between the Mainland and Taiwan, as well as the volume of transshipment cargo which were previously shipped via Hong Kong. Aviation, freight and tourism industries were likely to bear the brunt. HKTDC opined that the impact of the "Three Direct Links" policy on cross-strait trade and investment via Hong Kong should be limited because Taiwan companies using Hong Kong as a trade and investment platform, or operation hub, based their operations on practical needs rather than policy constraints. HKTDC believed that if Hong Kong maintained and enhanced its position as an internationally orientated financial and commercial centre in the region, it would benefit from the "Three Direct Links" policy in the long-term.

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<sup>6</sup> HKTDC set up an office in Taipei in December 2008 to promote trade and economic development between Hong Kong and Taiwan.

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## Other views

4.7 Meanwhile, industry practitioners, experts and academics were not optimistic about the future of Hong Kong and urged the Government to formulate countermeasures promptly. Tse Long, Vice-Chairman of the Container Transportation Employee General Union, estimated a 5% reduction in the container throughput of Hong Kong as a result of the "Three Direct Links" policy. Anthony Wong, President of the Hong Kong Logistics Association, predicted a 6% decrease in Hong Kong's container throughput per annum, i.e. over 1.38 million containers. Based on a handling fee of more than HK\$1,000 for each container, the "Three Direct Links" policy was expected to cost the local logistics industry more than HK\$1.3 billion a year. According to Professor Chen En of the Taiwan Research Institute of Xiamen University, Taiwan businessmen would make direct investments on the Mainland under the "Three Direct Links" policy and the role of Hong Kong as an intermediary would be significantly weakened. Chan Yan Chong, Director of the MBA Programme of the College of Business, City University of Hong Kong, pointed out that Hong Kong's tourism industry would be adversely affected by the competition from its Taiwan counterparts because of the implementation of the "Three Direct Links" policy.

## **5. Taiwan's economic stimulus measures**

5.1 Facing the impact of the financial tsunami, the Taiwan authority has introduced a number of economic stimulus measures to boost economic growth. The measures can be categorized into 10 different groups, namely improving overall competitiveness, increasing public construction investment, encouraging private investment, boosting consumption, supporting small and medium enterprises (SMEs), expanding export markets, facilitating short-term employment, cutting taxes, protecting deposits and implementing accommodative monetary policy. Details of the measures are set out in the following paragraphs.

### Improving overall competitiveness

5.2 The Taiwan authority has implemented the "Plan to Increase the Ceiling on Mainland-bound Capital Investment and Simplify Investment Review Procedures" to relax officially the capital restriction on Mainland investments from Taiwan companies, so as to strengthen Taiwan's participation in the global economy and improve overall competitiveness. The ceiling is relaxed from 40% to 60% of the combined net worth, while the cap for individual investment on the Mainland is lifted from NT\$80 million (HK\$20.32 million)<sup>7</sup> to US\$5 million (HK\$38.94 million) annually.

5.3 Meanwhile, the Taiwan authority has streamlined the vetting procedures for Mainland-bound investment of Taiwan companies. For investment valued below US\$1 million (HK\$7.79 million), applications can be filed within six months after the investment is made. Only cases with an accumulated investment value exceeding US\$50 million (HK\$389.35 million) are subject to review, while a streamlined approach is adopted for all the other cases.

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<sup>7</sup> The average exchange rate in 2008 was NT\$1=HK\$0.254.

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### Increasing public construction investment

5.4 The Taiwan authority has also increased public construction investment and expanded domestic demand in order to create more job opportunities. With the introduction of the "i-Taiwan 12 Projects", the Taiwan authority plans to invest an aggregate amount of around NT\$2,650 billion (HK\$673.1 billion) between 2009 to 2015 and expects to create 120 000 jobs each year. The annual economic growth rate will also increase by 1.2%. The main focuses of the "i-Taiwan 12 Projects" include establishing a fast and convenient islandwide transportation network, building the Taoyuan International Air City, developing a high-tech industrial cluster, revitalizing the city of Kaohsiung, promoting the natural products industry and green tourism, as well as developing the infrastructure of offshore islands.

### Encouraging private investment

5.5 In order to encourage private investment and revitalize the economy, the Taiwan authority has launched the "Sky-Net Project" as a major initiative to create global business opportunities. The target is to attract US\$8.5 billion (HK\$66.2 billion) in 2009, in the hope of channelling foreign investment to the manufacturing and public construction sectors. For the manufacturing sector, key promotion industries are optoelectronics, semiconductors, iron and steel, as well as petroleum and chemical products. As regards the public construction sector, promotion efforts focus on the "i-Taiwan 12 Projects".

### Boosting consumption

5.6 The Taiwan authority is fully committed to boosting consumption and invigorating economic activities. In January 2009, every Taiwan citizen, whether rich or poor, received NT\$3,600 (HK\$914) worth of consumer vouchers<sup>8</sup>, which would expire at the end of September 2009. The consumer vouchers are estimated to cost about NT\$85.7 billion (HK\$21.8 billion), of which 2.24%, or NT\$1.92 billion (HK\$490 million), is administrative cost.

5.7 On the effectiveness of consumer vouchers in stimulating the economy, the Taiwan authority estimates that the initiative will bring about a 0.66% economic growth in 2009. According to some retailers, the vouchers have helped boost turnover during the Chinese New Year. However, it will take a quarter to observe before the effectiveness of these vouchers in enhancing consumer sentiment can be confirmed.

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<sup>8</sup> The NT\$3,600 worth of consumer vouchers comprises six NT\$500 vouchers and three NT\$200 vouchers.

### Supporting small and medium enterprises

5.8 Difficulty in raising funds poses the greatest challenge to SMEs amid the financial tsunami. In this connection, the Taiwan authority has repeatedly injected capitals into the banking system and urged the banks to extend loans to SMEs. Apart from this, the authority provides the Taiwan Business Bank<sup>9</sup> with stand-by credit so that the latter can underwrite more SME loans for use as daily working capital and machinery procurement. The Taiwan Business Bank offers concessionary lending rate as low as 2.2% per annum.

5.9 The Taiwan authority has also increased the guarantees provided under the "Small and Medium Enterprise Credit Guarantee Fund of Taiwan" by offering an extra 10% guarantee on average, thus raising the guarantee ceiling from the previous 40%-70% to as high as 80%. The maximum amount of guaranteed loans for SMEs is increased from NT\$100 million (HK\$2.54 million) to NT\$120 million (HK\$3.05 million). The processing of claims from banks is also expedited to increase their incentive to grant loans to SMEs.

### Expanding export markets

5.10 Taiwan has implemented the "New Cheng Ho Plan" to assist manufacturers in expanding the export market. The Taiwan authority plans to allocate a total of NT\$8.5 billion (HK\$2.16 billion) between 2009 and 2012 to support exporters in five specific directions as follows:

- (a) providing concessionary export loans and export insurance;
- (b) stepping up efforts in developing markets such as the Mainland, India, Russia, Brazil, the Middle East and the ASEAN region,
- (c) funding Taiwan businesses in export promotion and participation in exhibitions;
- (d) helping foreign businesses purchase more Taiwan products; and
- (e) supporting Taiwan companies in securing procurement contracts from foreign governments.

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<sup>9</sup> The Taiwan Business Bank is the largest bank for SMEs in Taiwan.

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### Facilitating short-term employment

5.11 As the impact of the global financial tsunami has spread to the labour market, short-term employment initiatives costing NT\$9.3 billion (HK\$2.36 billion) have been introduced to alleviate unemployment, with 69 000 job opportunities anticipated. The short-term employment opportunities include checking for catch-water blockage, taking care of students with intellectual disabilities, processing of recovered resources and offering quality tourism services. Priorities are given to elderly workers, women, indigenous residents and university graduates with no working experience. Employment periods will last no longer than eight months.

5.12 The Taiwan authority has launched the "Plan of Promoting Employment Skill in Short-term" to encourage enterprises to introduce no-pay leave instead of laying-off employees. Enterprises offering no-pay leave to their employees may apply for government funding to organize vocational training courses. The government may grant a 100% subsidy on the related expenses. The subsidy ceilings for large enterprises and SMEs are NT\$1.9 million (HK\$480,000) and NT\$950,000 (HK\$240,000) respectively. Employee participants are also entitled to receive a salary allowance of up to NT\$10,000 (HK\$2,540) per month for a maximum of six months. The Taiwan authority estimates that the expenses incurred will be around NT\$16 billion (HK\$4.06 billion) and about 170 000 workers will be benefited.

### Cutting taxes

5.13 In response to the economic downturn, the Taiwan authority has raised the amounts of four types of tax deductions and allowances to alleviate the burden on taxpayers, including a deduction in individual income tax standard rate and salary tax, an increase in allowances for the disabled or handicapped, and education expenses. Under the new tax rate, each household may save an amount ranging from NT\$7,300 (HK\$1,854) to NT\$49,000 (HK\$12,446) in taxes. The tax revenue of the Taiwan authority will be reduced by NT\$35 billion (HK\$8.89 billion). It is estimated that about 3.8 million households, or half of the 7.5 million households in Taiwan, will benefit from the tax cuts. Based on the figure of 5.31 million tax-filing households in 2009, nearly 70% of them will pay less tax. This tax cut programme has been the largest tax cut programme in Taiwan in recent years. The people of Taiwan generally welcome the move and believe that it will be of much help to the middle and lower income groups.

5.14 Furthermore, in order to promote car sales and conserve energy, concessionary rate for excise tax is applicable to new passenger cars (2 000 c.c. or below) purchased before the end of 2009, with the amount of excise tax fixed at NT\$30,000 (HK\$7,620) per car.

### Protecting deposits

5.15 The Taiwan authority has provided a 100% deposit protection scheme from 7 October 2008 to the end of December 2009. This arrangement is to enhance public confidence in making deposits and stabilizing the monetary system.

### Implementing accommodative monetary policy

5.16 The accommodative monetary policy implemented by the Taiwan authority is conducive to reducing borrowing costs. Since September 2008, the central bank of Taiwan has repeatedly injected capitals into the banking system and has lowered the discount rate seven times to the current level of 1.25%, an accumulated reduction of 2.25%.

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