

**CENTRAL POLICY UNIT
HONG KONG SPECIAL ADMINISTRATIVE REGION**

**CONSULTANCY STUDY ON
SOCIAL, ECONOMIC AND POLITICAL
DEVELOPMENTS
IN THE MAINLAND,
WITH PARTICULAR EMPHASIS ON
REGIONAL DEVELOPMENTS AND
THE GUANGDONG PROVINCE**

FIRST BI-MONTHLY REPORT

**TEAMONE ECONOMIST LIMITED
12 FEBRUARY 2008**

EXECUTIVE SUMMARY

1. Implications of the 17th CPC Congress to Hong Kong

The 17th CPC Congress was held on October 15-21, 2007. The “scientific concept of development” proposed by Party General Secretary Hu Jintao set the scene and provided guidance for the future development of the country. This concept of development, which started at the beginning of the Eleventh Five-Year Plan in 2006, focuses on the holistic improvement of the society and “coordinated development”; giving priority to “balanced” and “quality” growth. Given that China’s per capita GDP has risen four times between 1980 and 2000, Hu Jintao targets for another quadrupling of per capita GDP between 2000 and 2020 level. This implies 40 consecutive years of rapid growth for China, a trend not seen in the rise of any major economy in the past. The 17th CPC Congress also included objectives related to coordinated development among regions. The positioning of coastal, central, western regions were re-established. Hong Kong should get familiarized with such a direction of development, closely follow the changes in government officials, such as Wang Yang’s designation as the Secretary of the Guangdong Provincial CPC Committee, so that communication with the Mainland can be strengthened.

2. The direction for implementing the stock market “through-train” scheme

Although the implementation of the stock market “through-train” scheme has been stalled, given that problems arising from excess liquidity in the Mainland have already triggered a surge in asset prices and ignited inflationary pressures, allowing private sector funds from the Mainland to formally enter Hong Kong is just a matter of time. Still, before the “through-train” kicks off, the relevant risks and operating mechanics involved need to be carefully assessed in order to protect investors from incurring losses due to large fluctuations in the market. At an appropriate time -- that is, when the Mainland is reasonably prepared with an alert system to safeguard financial security and control risk, in the education of its residents about the risks of investing in the Hong Kong stock market, as well as in providing them with market information and rights protection -- then “through-train” can be expected to start operation. Its exact scale, however, may be different from what was originally expected. It is widely believed that the “through-train” scheme will only be

implemented in stages and pilot-tested in a number of cities including Tianjin, Beijing, Shanghai, Guangzhou and Shenzhen, rather than be completely liberalized. This is consistent with the Mainland's practice whenever pilot schemes are introduced.

3. Yangtse River Delta's alternative energy industry takes shape

Facing mounting pressure from both tight energy supply and a growing need to protect the environment, the Yangtse River Delta (YRD) has aggressively developed "green energies" such as wind and solar power. In developing wind energy resources, Jiangsu and Zhejiang have grown rapidly, leading other Mainland provinces. Meanwhile, YRD is also continuing to seek rooms for developing solar power, bio-energy, geothermal energy, and small hydropower, etc. At the moment, Hong Kong and the Pearl River Delta (PRD) region continue to be plagued with air pollution, which mainly stems from the heavy flow of vehicles, ever-expanding business activities, and pollutants generated by power plants. YRD's alternative energy industry demonstrates a probable way to solve the problems of pollution in the greater PRD region. To be able to fundamentally resolve the problem of air pollution, Hong Kong needs to step up the development of renewable energies. Industry experts believe that there is much potential for Hong Kong to shift to the use of renewable energies -- wind power, in particular -- to generate electricity. Developing renewable energies in Hong Kong would not only be beneficial from an environmental protection point of view, but would also provide opportunities for Hong Kong businesses to expand their scope of investment in the Mainland. China has already grown to become the world's largest investor in renewable energies, the prospects for Hong Kong to invest in the Mainland's renewable energies sector is very promising.

4. Hebei's coastal ports to spur economic development in Beijing-Tianjin-Hebei and the central and western hinterland: underlying opportunities

Riding on the opportune time when the Mainland is aggressively promoting the development of the Bohai Rim region, Hebei will make full use of its unique coastal position, which embraces both Bohai Rim and Beijing-Tianjin area, to speed up the development of its ports of Qinhuangdao, Jingtang, Huanghua, and Caofeidian. To be able to strengthen the interaction between the coastal region and hinterland and

accomplish its objective to become a socially- and economically-advanced province, Hebei has undertaken the construction of a comprehensive transport link that would promote the interaction between its eastern coastal regions with the Mainland's northern and northwestern regions, as well as with Beijing-Tianjin, Shaanxi, Shanxi, Inner Mongolia and the northern areas of Henan. This would promote rapid growth in trade between these areas with overseas markets and trigger a surge in demand for logistics services, providing Hong Kong's logistics enterprises with vast business opportunities. The actual impact, however, needs to be confirmed by industry players. Without the government's active promotion, the potential problems that Hong Kong's logistics enterprises may face cannot be underestimated, as Hebei is located quite a distance from Hong Kong.

5. The restructuring of Guangdong economy and its impact on Hong Kong

Guangdong has taken an important move towards a heavy-industry-based economy. The value-added of three emerging industries (electronics, machinery and petrochemicals) has grown to account for 46% of the province's total value-added of industries, while the share of the three traditionally most competitive industries (textiles, food and building materials), in which Hong Kong manufacturers excel, has dropped to 17.2%. The trend shows that as Guangdong's heavy industries takes off, Hong Kong manufacturers are facing increasing challenges to keep their leading position by the traditional industries, and will eventually be forced to make a decision between relocating to the central or western regions and moving up the value-added ladder. Aside from the manufacturing sector, the restructuring of Guangdong's industries would also lead Hong Kong's services sector towards a new stage of development. With Guangdong's industrial development now focused on transforming into a suitably higher-value-added and heavy-industry-based economy, the demand for producer services related to the heavy industries and high-technology sector would simultaneously increase, leading the services sector towards further development. As the main conduit for Guangdong enterprises to have access to the overseas markets, it is meaningful for Hong Kong to enhance the competitiveness of both sides and better promote the development and transition of its services industries, by appropriately integrating its networks in international finance, information and trade with Guangdong's supply chains of heavy and high-tech industries.

6. Guangdong promoting the relocation of industries from the Pearl River Delta towards the mountain and outlying areas: opportunities for Hong Kong

Endowed with relatively rich resources while the cost of production is kept low, the mountain areas as well as the eastern and western outskirts of Guangdong are hinterlands for Guangdong's economic development. Promoting the relocation of industries from the Pearl River Delta (PRD) to these areas would help Hong Kong enterprises in the PRD lower their operating costs, and give the PRD bigger room to develop higher-end industry segments. As Hong Kong enterprises step up their levels of cooperation with the PRD, they should also look into relocating their investments to the mountain areas and outskirts of Guangdong, develop resource-based and unique processing industries as well as labour-intensive marine, energy and petrochemical industries, and consider new modes of jointly developing industrial parks in these regions to house the relocating industries. In accordance with Guangdong's need for industrial restructuring, Hong Kong businessmen could also expand and step up cooperation with the mountain areas and outskirts to transfer appropriate technologies to these regions. As an international port, Hong Kong has a clear edge in providing a platform for coordinating technical resources and services. Hong Kong enterprises and other related technology-related institutions can strengthen cooperation with the hinterland in the areas of electronics and information technology, petrochemicals, bio-pharmaceuticals and other high-end technologies.

7. Implementation of Meizhou's four development strategies yield opportunities for Hong Kong's business and professional services

To spur economic development in Meizhou, the city has aggressively adopted the four strategies of "opening up Meizhou, industrializing Meizhou, building an ecological Meizhou, and building a cultural Meizhou". In recent years, Meizhou has actually witnessed rapid development in its transportation infrastructure, narrowing its distance from other more developed Pearl River Delta areas, Jiangxi, and Fujian. This has created vast potentials for Meizhou to develop into a major transport hub and regional distribution center serving Fujian, Guangdong, Jiangxi and the Pan Pearl River Delta region. According to the objectives of "Four Meizhou", the city would develop into a supply base of raw materials and agricultural products for advanced coastal economies, a modern manufacturing base, a regional business and logistics hub, and a backyard for tourism and leisure

activities. To achieve these, Meizhou will have to rely on external professional and financial support, giving rise to opportunities for Hong Kong businesses. By actively participating in the development and cultivation of the various industries of Meizhou, Hong Kong's businesses will play a unique role in the city's sustainable development.

8. "Industrializing Maoming" and "Achieving Four Leaps" and opportunities for Hong Kong

Maoming is currently in the process of "industrializing the city" and "achieving four leaps", with an aim of turning the city into a major economic city in western Guangdong and become the largest heavy and chemical industrial base in the Pan-PRD region. Maoming is actually an important city in western Guangdong, with strong development potential in the energy, industrial, agricultural and services sectors. With closer cooperation, Maoming and Hong Kong could achieve win-win. In particular, Hong Kong enterprises can seek opportunities in the areas of downstream petrochemicals, agricultural goods production and processing, information networking, and technology development services. One of the hindrances to closer cooperation between Maoming and Hong Kong lies in the geographic distance between the two. Despite the rapid development of highways in western Guangdong, the travel distance involved remains far. Strengthening cooperation between the two sides may still require active promotion by the government.