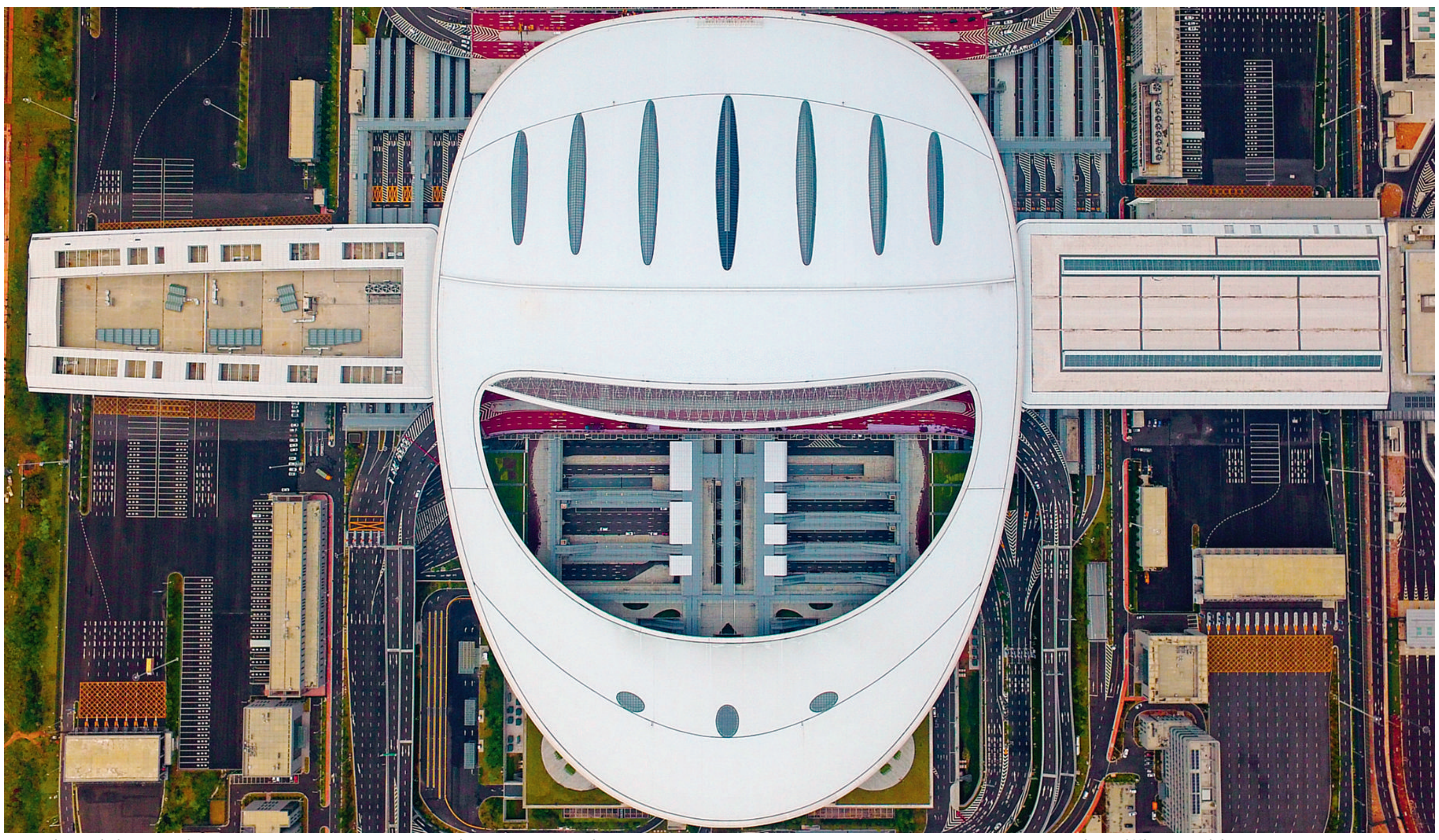
BACK TO BUSINESS

THE VIEW

CHRISTER LJUNGWALL AND SIYANG LI

HK must adapt or fall

China's ascendancy on the world stage and its plans for future could mean devastation and ruin for city's gateway role into country



Zhuhai Port is just one link between Hong Kong and the mainland, but such links, as the Greater Bay Area takes shape, could put Hong Kong in a difficult position. Photo: Xinhua

At the heart of China's future development is Beijing's long-term plan to turn the Greater Bay Area into an economic powerhouse. Such a plan puts Hong Kong's current position under pressure, as alternative locations will soon provide legal and financial services similar to those found in the city.

Thus, its position depends very much on China's economic and social conditions, particularly its progress in reform and opening up.

A vision for Hong Kong is also of vital importance, and this lies in the hands of those who lead the city.

Historically, Hong Kong's legal system and economy have operated outside the direct influence of the mainland. Because of this institutional setting, the city has been a semi-independent window for the mainland since before the 1997 handover.

The country lagged behind advanced societies in science, technology and economic openness. Even before its modernisation, Chinese authorities took a closed-border approach to foreign influence, and so international exchange in information and culture was limited.

In the Qing era, Guangdong operated China's only ports to receive foreign goods. It had no institutionalised customs system in place until 1685, when emperor Kangxi lifted the ban on maritime trade and opened the ports to foreign traders.

As an outpost for China, Hong Kong has gone through a tumultuous transformation. In the 1800s, the British saw the potential of Victoria Harbour even though Hong Kong at the time had only a few thousand residents and was largely wilderness.

In 1842, the Qing government ceded Hong Kong Island to the British crown under the Nanjing treaty, and that ushered in the rise of Hong Kong's economic and political status. It became an important trading post with a high volume of inbound and outbound cargo.

Even the Japanese occupation during World War II did not fundamentally alter Hong Kong's position. During the Sino-Japanese war, from 1937 to 1945, both the nationalist and communist parties used Hong Kong's special political and geographical position to conduct foreign affairs and facilitate travel.

> **For the central government and China's long-term strategy, it is extremely risky to bet too much on Hong Kong**

With its relatively extensive political freedom and openness to the movement of goods and people, Hong Kong emerged as an international financial centre with some of the highest standards of living in the world.

Today, as Beijing deepens its reforms and continues to open up, it is bound to put forward a new development strategy. It plans to create a dynamic world-class region comprising a cluster of innovative cities by 2022 in the Greater Bay Area. By 2035, the plan is that the region will have developed a first-rate system to support a knowledge-driven economy.

By the 100th anniversary of the People's Republic of China in 2049, the goal is for the country to be a world leader in higher education, research, advanced manufacturing and service production. Of critical importance for this development is a legal system conducive to trade, investment and doing business.

Another vital component is a diversified and competitive financial sector, which in turn relies on a convertible currency and minimal currency restrictions.

The list of necessary reforms is long. One main question, however, is whether the central government is likely to go ahead with this tremendously important development while being dependent on a Hong Kong that may be paralysed by violent demonstrations and protests. The answer is, probably not.

For the central government and China's long-term strategy, it is extremely risky to bet too much on Hong Kong. This is obvious in view of the recent developments in the area. Rebalancing the economic and financial power among the different regions within the Greater Bay Area is the most natural path to take.

For Hong Kong, it is time to think about its position in a swiftly changing environment. Traditional factors supporting its growth and prosperity are under threat, with its role as a window for mainland and foreign exchange fading in importance. Meanwhile, social instability is wreaking havoc from the inside.

Seeing all these risks and opportunities, the central government may gradually and consciously weaken Hong Kong's special position in the nation's overall development plan, and implement reform measures that shape new alternatives in cities such as Shenzhen, Guangzhou, Zhuhai and Macau, to build a more diversified portfolio.

Soon, the conditions for trade, investment and running businesses will converge in the Greater Bay Area, which is also in line with Beijing's intention to bridge the gap of development among regions. The changes will be fast and significant.

Hong Kong's immediate concern will be to ensure a well-balanced adaptation to these new circumstances. What are the comparative and competitive advantages, if any? How should Hong Kong begin the process of enhancing its current major industries to match the onslaught of new competition?

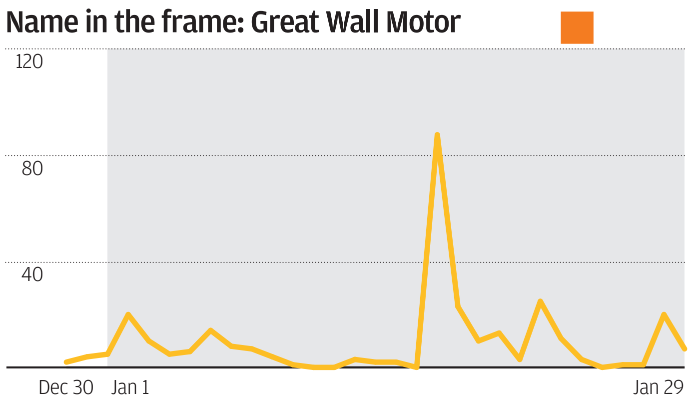
The consequences for a Hong Kong that does not respond to the pressure for change will be devastating. It will find itself in an untenable position just a few years from now. The need for leadership is dire.

Christer Ljungwall is an economist with long-standing research experience of China. Siyang Li is a PhD candidate with Peking University HSBC Business School majoring in economics. Political scientist Mikael Román also contributed to this article

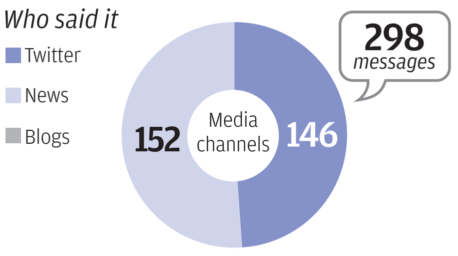
MARKET TALK

A NEW JOURNEY

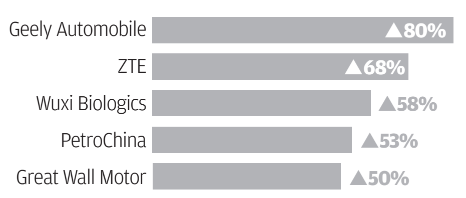
Name in the frame: Great Wall Motor



Who said it



Hot companies in the market



Source: Sentifi.com

Analysis of the most talked about stocks in Hong Kong and the mainland. Get it in real time on scmp.com/Business

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BloombergQuint
China's largest SUV maker Great Wall Motors Ltd. will showcase various products and technologies at the Auto Expo 2020 in Greater Noida, Delhi NCR, next month as part of its launch in the Indian ma...

Note: All data as at 6pm yesterday SCMP

MACROSCOPE

AIDAN YAO

China's economy will start solidly in 2020 then lose steam

GDP data and trade deal bode well, but tight financial conditions and US import commitments will weaken growth in the second half

Global markets got off to a positive start in 2020, with risky assets hitting new highs. Two macro factors contributed to this strength: tentative signs of the global economy bottoming out and the US-China phase one trade deal helping to remove risks. Let's examine both developments in the context of China.

First, the latest gross domestic product data showed that the Chinese economy stabilised at 6 per cent in the fourth quarter of 2019, arresting the persistent growth deceleration of the first three quarters of last year.

The services sector continued to deliver a solid performance, expanding at 6.9 per cent. But it was the acceleration of the industrial and manufacturing sector – to 5.7 per cent from 5.6 per cent – that accounted for most of the upside surprise in fourth-quarter GDP data. The expenditure breakdown showed decent growth from consumption, while the investment contribution also improved. The balance of growth may shift modestly further in early 2020, but not enough to alter the structural trends in the economy.

Industrial production growth also rebounded strongly to 5.9 per cent in the fourth quarter from 5 per cent, thanks to improved corporate profitability and factory-gate prices. With inventory levels at multi-year lows, improved final demand and easing trade tensions could strengthen the growth momentum further.

Part of this growth impulse emanated from offshore. China's export growth quickened noticeably in December. While the base effect flattered the annual comparison, there is corroborating evidence of the global trade cycle bottoming from other export bellwethers in Asia.

As the US and China have also sealed their phase one deal, dissipating uncertainties could further strengthen the global trade recovery. We expect China's exports to resume growth in 2020, although their contribution to GDP could be offset by increased imports from the US as required by the phase one deal.

Compared to the brighter external picture, the domestic economy appears to be in "steady as she goes" mode. Consumer spending held its ground, maintaining 8 per cent growth in December, despite the record Singles' Day sales in November that stimulated consumption of big-ticket items. The latter could also be a result of lower turnover in the housing market. Indeed, a long-overdue downturn in housing construction could play out in 2020, making it a key risk for the economy.

Fortunately, capital expenditure growth by manufacturers appears to have found a floor. The current soft patch in infrastructure investment is likely to give way to a modest recovery. The combination of rising manufacturing and infrastructure investment should help offset weaker real-estate construction, keeping total investment growth broadly stable in 2020.

Overall, there is scope for the current cyclical rebound to extend in the coming months.

Beyond the short-term respite, however, we think various structural impediments will return to the fore and cause renewed growth headwinds in the second half of the year. Internally, still-tight financial conditions – partly engineered by Beijing to deleverage the economy – are expected to dampen domestic demand.

> **Will Beijing insist on pleasing the US by sacrificing its relations with others or endure slower growth?**

This is likely to render the modest reductions in the loan prime rate inadequate and open the door for the People's Bank of China to resume reserve requirement ratio cuts, and for Beijing to add fiscal support.

The risks of the US-China trade dispute resurfacing are not small, given the purchase commitments to which China has agreed. Fully meeting those commitments will more than double China's imports from the US over the coming two years. With little chance that this can be absorbed by a natural increase in demand, China will either have to reduce imports from elsewhere, which would risk antagonising other trading partners, or substitute for domestic production, which would slow economic growth.

Neither outcome is ideal. The question is: will Beijing insist on pleasing the US by sacrificing its relations with others or endure slower growth?

Factoring in some of these risk factors has led to our cautious view about the Chinese economy in 2020. We expect a solid first half to give way to renewed weakness in the second half of the year, leaving full-year growth at 5.8 per cent.

Aidan Yao is senior emerging Asia economist at AXA Investment Managers

CURRENCY CALCULATOR

Figures are mid-price TT rates provided by HKAB

January 29, 2020	Aust	Britain	Canada	China	Euro	HK	India	Japan	Korea	Mal	NZ	P'stan	Phil	S'pore	S Africa	Switz	Taiwan	Thai	US
Australia $		0.5192	0.8902	4.709	0.6134	5.260	48.14	73.80	794.8	2.759	1.035	104.67	34.32	0.9183	9.836	0.6581	20.29	20.83	0.6764
Britain £	1.926		1.715	9.07	1.181	10.13	92.72	142.1	1531	5.314	1.992	201.59	66.10	1.769	18.94	1.267	39.07	40.12	1.303
Canada $	1.123	0.5832		5.289	0.6891	5.908	54.08	82.90	892.8	3.099	1.162	117.58	38.55	1.032	11.049	0.739	22.79	23.40	0.7598
China Rmb	0.212	0.1103	0.1891		0.130	1.1170	10.224	15.67	168.8	0.5860	0.2197	22.229	7.289	0.1950	2.089	0.1398	4.309	4.424	0.1436
Euro €	1.630	0.8464	1.451	7.676		8.574	78.48	120.3	1296	4.498	1.686	170.63	55.95	1.497	16.034	1.073	33.07	33.96	1.1026
Hong Kong $	0.1901	0.0987	0.1693	0.895	0.1166	1	9.153	14.03	151.1	0.5246	0.1967	19.900	6.525	0.1746	1.870	0.1251	3.857	3.960	0.1286
India R	0.0208	0.0108	0.0185	0.0978	0.0127	0.1093		1.533	16.51	0.0573	0.0215	2.174	0.713	0.0191	0.2043	0.0137	0.4214	0.4327	0.0140
Japan ¥	0.0136	0.0070	0.0121	0.0638	0.0083	0.0713	0.6524		10.77	0.0374	0.0140	1.418	0.4651	0.0124	0.1333	0.0089	0.2749	0.2823	0.0092
South Korea W	0.0013	0.0007	0.0011	0.0059	0.0008	0.0066	0.0606	0.0928		0.0035	0.0013	0.132	0.0432	0.0012	0.0124	0.0008	0.0255	0.0262	0.0009
Malaysia RM	0.3624	0.1882	0.3226	1.707	0.2223	1.906	17.45	26.75	288.1		0.3749	37.94	12.44	0.3328	3.565	0.2385	7.353	7.55	0.2451
New Zealand $	0.9666	0.5019	0.8605	4.552	0.5930	5.084	46.54	71.34	768.3	2.667		101.18	33.18	0.8877	9.508	0.6361	19.61	20.14	0.6538
Pakistan R	0.0096	0.0050	0.0085	0.0450	0.0059	0.050	0.4600	0.7050	7.594	0.0264	0.0099		0.3279	0.0088	0.0940	0.0063	0.1938	0.1990	0.0065
Philippines P	0.0291	0.0151	0.0259	0.1372	0.0179	0.1533	1.4027	2.150	23.16	0.0804	0.0301	3.050		0.0268	0.2866	0.0192	0.5911	0.6069	0.0197
Singapore $	1.089	0.5654	0.9694	5.128	0.6680	5.728	52.43	80.36	865.5	3.005	1.127	113.99	37.38		10.7111	0.7166	22.09	22.68	0.7366
South Africa rand	0.1017	0.0528	0.0905	0.4787	0.0624	0.5348	4.895	7.50	80.8	0.2805	0.1052	10.642	3.489	0.0934		0.0669	2.063	2.118	0.0688
Switzerland Sfr	1.520	0.7890	1.3528	7.156	0.9322	7.993	73.16	112.14	1207.8	4.193	1.572	159.06	52.15	1.395	14.947		30.83	31.65	1.0278
Taiwan $	0.0493	0.0256	0.0439	0.2321	0.0302	0.2593	2.373	3.637	39.18	0.1360	0.0510	5.159	1.692	0.0453	0.4848	0.0324		1.027	0.0333
Thailand Bt	0.0480	0.0249	0.0427	0.2261	0.0294	0.2525	2.311	3.543	38.16	0.1325	0.0497	5.025	1.648	0.0441	0.4722	0.0316	0.9740		0.0325
US $	1.478	0.7676	1.32	6.962	0.907	7.776	71.18	109.11	1175	4.079	1.529	154.75	50.74	1.358	14.54	0.973	30.00	30.80	

US$ MARKET RATES

	Bid	Ask
HK ($)	7.7721	7.7725
Japan (¥)	109.1400	109.1600
Euro (€) *	1.0994	1.0997
UK (£) *	1.2998	1.3000
Switzerland (SFr)	0.9761	0.9763
Canada (C$)	1.3186	1.3188
Australia (A$) *	0.6749	0.6750
China (yuan)	6.9364	6.9369
Indonesia (Rup)	13,620	13,635
Malaysia (RM)	4.0795	4.0815
Philippines (peso)	50.8550	50.8750
New Zealand (NZ$) *	0.6515	0.6519
Singapore (S$)	1.3611	1.3613
S Korea (won)	1,178.42	1,179.45
Taiwan (NT$)	30.0970	30.1070
Thailand (baht)	30.9300	30.9700
India (rupee)	71.2847	71.3237
S Africa (rand)	14.5791	14.5831

* per unit. Rates at 10.15pm.

KEY LENDING RATES

HK prime	5.000%	UK bank base	0.750%
US fed fund	1.750%	Euro prime	0.250%
US prime	4.750%	Tokyo prime	1.475%
Taiwan prime	2.616%	S'pore prime	5.250%