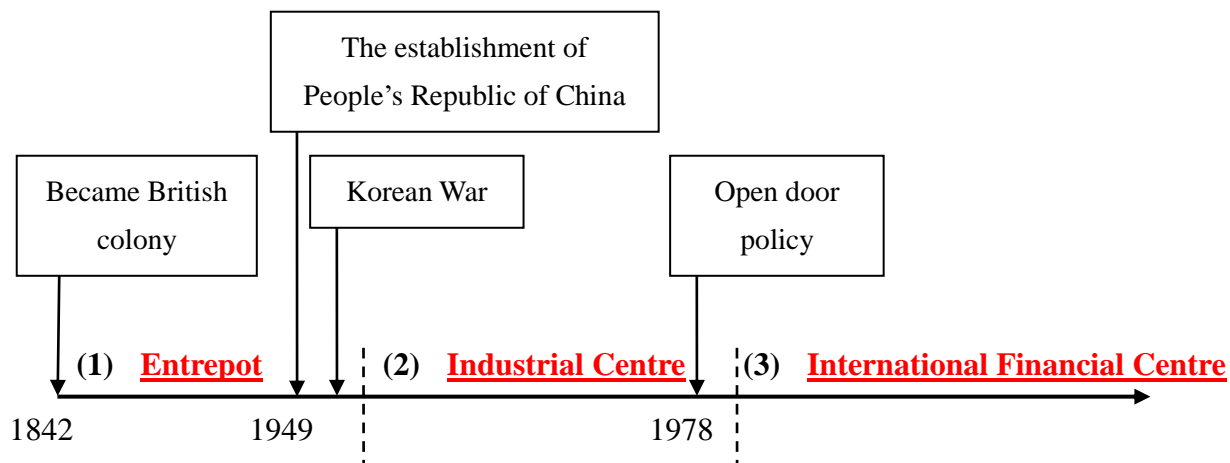


## Chapter 1 Hong Kong Business Environment

### 1. Overview of Hong Kong Economy

#### 1.1 Development of Hong Kong Economy



#### 1.2 Classification of Economic Sectors

Sector	Definition	Examples
Primary production	Direct extraction of (4) <b><u>natural resources</u></b>	Farming, mining and fishing
Secondary production	Turing (5) <b><u>raw materials</u></b> into finished or semi-finished goods	Manufacturing or construction
Tertiary production	Provision of different kinds of (6) <b><u>services</u></b>	Tourism, financial services

### 1.3 Economic Sectors in Hong Kong

	Primary Production	Secondary Production	Tertiary Production
Contributed to GDP in 1991	0.3%	22%	77.8%
Contributed to GDP in 2011	< 0.1%	6.8%	93.1%
Proportion	(7) <u>Smallest</u>	(8) <u>In between</u>	(9) <u>Largest</u>
Trend	(10) <u>Decreasing</u>	(11) <u>Decreasing</u>	(12) <u>Increasing</u>

\*Gross Domestic Product (GDP) measures the total value of all the goods produced in a country/territory in a specified period. It is a common measure to assess the performance of an economy.

### 1.4 Characteristics of Hong Kong Economy

Characteristics	Description
Lack of (13) <u>primary production</u>	<ul style="list-style-type: none"> <li>• Lack of natural resources in Hong Kong</li> <li>• Contribute less than 1% of GDP</li> </ul>
Concentration on (14) <u>tertiary production</u>	<ul style="list-style-type: none"> <li>• Hong Kong transformed into a service-oriented economy since 1980s</li> <li>• Contribute over 90% of GDP</li> </ul>
Free trade	<ul style="list-style-type: none"> <li>• No (15)<u>import quota</u> on goods and (16)<u>tariff-free</u></li> <li>• Little government intervention to the market</li> </ul>

Dependence on external trade	<ul style="list-style-type: none"> <li>Total value of trade was equal to more than 430% of Hong Kong's GDP in 2012</li> <li>The Hong Kong economy is affected by the changes in external economic conditions</li> </ul>
(17) <b>Simple</b> taxation system	<ul style="list-style-type: none"> <li>Only three (18)<b>direct taxes</b> in Hong Kong</li> <li>Low tax rates</li> </ul>
Large number of small and medium enterprises (SMEs)	<ul style="list-style-type: none"> <li>SMEs made up of 98% of Hong Kong's business units</li> </ul>

### 1.5 Contributions of Businesses to Hong Kong Economy

- Providing goods and services
- Improving standard of living
- Providing employment opportunities
- Raising productivity
- Source of government revenue

### 1.6 Recent Development of Hong Kong Economy

<b>Trend</b>	Transforming into a knowledge-based economy
<b>Definition of knowledge-based economy</b>	An economy that is directly based on the (19) <b>production</b> , (20) <b>distribution</b> and the (21) <b>use</b> of knowledge and information
<b>Features of knowledge-based economic activities</b>	Involve mainly the use of knowledge, creativity and design
<b>Examples of knowledge-based economic activities</b>	Fashion design, film production and information technology

Four key industries in Hong Kong			
Financial services	Trading and logistics	Tourism	Producer and professional services

Six priority industries		
Cultural and creative industries	Medical services	Education services
Innovation and technology	Testing and certification services	Environmental industries

## **2. Economic Relationship between Hong Kong and the Mainland**

### **2.1 The Mainland, the Largest Trading Partner of Hong Kong**

- The Mainland is the biggest market for Hong Kong's imports and exports. It is the largest trading partner of Hong Kong.

### **2.2 Flow of Capital between Hong Kong and the Mainland**

- With the free flow of capital and comprehensive (22)**financial system**, Hong Kong becomes the platform for Mainland enterprises to raise international funds.
- More than 700 Mainland enterprises are listed on the Hong Kong (23)**stock market**.

### 2.3 Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA)

<b>Background</b>	<ul style="list-style-type: none"><li>• Signed in 2003</li><li>• The first free trade agreement ever concluded by the Mainland and Hong Kong</li></ul>
<b>Areas covered</b>	<ul style="list-style-type: none"><li>(a) Reduce (24)<u>barriers to trade</u> in goods<ul style="list-style-type: none"><li>• Over 1,000 categories of Hong Kong-made products are tariff-free when they are exported to the Mainland</li></ul></li><li>(b) Promote free trade in (25)<u>services</u><ul style="list-style-type: none"><li>• Reduce restrictions on Hong Kong-based (26)<u>service providers</u> that start their business in the Mainland</li><li>• Sign agreements on the recognition of professional qualifications</li></ul></li><li>(c) Facilitate cross-border trade and investment<ul style="list-style-type: none"><li>• Co-operate in areas such as custom clearance facilitation, co-operation on branding and protection of (27)<u>intellectual property</u></li></ul></li></ul>

## 2.4 Pan-Pearl River Delta Regional Cooperation Framework Agreement

<b>Year of signature</b>	2004
<b>Parties involved</b>	Macau and nine provinces/regions in the Mainland
<b>Objectives</b>	Increase the economic influence and competitiveness, and speed up the economic co-operation and development within the Pan-Pearl River Delta Region
<b>Contributions to Hong Kong economy</b>	It strengthens the economic ties between Hong Kong and the Mainland. For example, a transportation network will be built to connect Hong Kong and the Mainland

## 3. Globalisation and Hong Kong Economy

### 3.1 What is Globalisation?

<b>Origin</b>	In 1980s and early 1990s
<b>Definition</b>	<ul style="list-style-type: none"><li>• The reduction and removal of barriers between national borders in order to facilitate the flow of (28)<b>goods</b>, (29)<b>capital</b>, (30)<b>services</b> and (31)<b>labour</b></li><li>• People in the world are unified into single society and they affect one another</li></ul>
<b>Causes</b>	Liberalisation of trade, improvement in telecommunications and transportation networks

### 3.2 Impacts of Globalisation on Hong Kong Businesses

Impacts on businesses	Descriptions
Expansion of overseas market	<ul style="list-style-type: none"> <li>• Businesses can build up sales network all over the world more easily</li> <li>• Stimulate the development of (32)<u>multinational corporations</u></li> </ul>
Global sourcing and outsourcing	<ul style="list-style-type: none"> <li>• Businesses outsource production processes to foreign subcontractors to reduce (33)<u>production cost</u> and take advantage of skills and technologies possessed by foreign subcontractors</li> <li>• Businesses can purchase raw materials and goods that are not available locally in foreign countries</li> </ul>
Transfer of technology	<ul style="list-style-type: none"> <li>• Businesses bring technology to other countries when they set up branches overseas</li> </ul>
International flow of information and capital	<ul style="list-style-type: none"> <li>• Businesses can obtain up-to-date information on the (34)<u>internet</u> and make business decisions</li> <li>• Businesses can allocate funds to different markets due to the reduction in the barriers to trade in goods and services</li> </ul>
Keen (35) <u>competition</u>	<ul style="list-style-type: none"> <li>• Foreign goods can be imported to the local market more easily</li> <li>• Multinational corporations take advantage of the (36)<u>economies of scales</u> to reduce average production costs and compete with local businesses</li> </ul>

### 3.3 Major International Trade Organisations

Organisation	Members	Objectives
<p>(37) <u>World Trade Organization</u> (WTO)</p>	<p>159 members in the world</p>	<ul style="list-style-type: none"> <li>• Break through trade barriers and allow foreign trade to enter domestic market</li> <li>• Platform for sorting out trade problems among member governments</li> </ul>
<p>(38) <u>Asia-Pacific Economic Cooperation</u> (APEC)</p>	<p>21 members including Hong Kong, China, Australia, USA</p>	<ul style="list-style-type: none"> <li>• Pool resources within the Asia-Pacific region</li> <li>• Strengthen members' economies and achieve efficiency</li> </ul>



#### 4. Factors Affecting Business Decisions

Factor	Description	Hong Kong's situation
<b>Economic</b>	<ul style="list-style-type: none"> <li>• <b>Trade policy:</b> Trade barriers hinder trade and business activities</li> <li>• <b>Overall economic environment:</b> Businesses expand when the economy is prosperous</li> <li>• <b>Interest rate:</b> A rise in interest rate reduces businesses' incentive to borrow a loan.</li> <li>• <b>Rental level:</b> It is one of the main operating expenses to a business</li> </ul>	<ul style="list-style-type: none"> <li>• Adopted (39)<b>free trade</b> policy which encourages inflow of foreign capital</li> <li>• Hong Kong is an (40)<b>externally-oriented</b> economy, which is greatly affected by external economic conditions</li> <li>• High rental level drives many local businesses out of the market</li> </ul>
<b>Political</b>	<ul style="list-style-type: none"> <li>• Stable political environment provides greater protection for businesses' investments</li> <li>• Political unrest discourages businesses from making investments.</li> </ul>	<ul style="list-style-type: none"> <li>• As Hong Kong is politically stable, foreign businesses find it safe to make investments there</li> </ul>

<p><b>Legal</b></p>	<ul style="list-style-type: none"> <li>• Clear set of (41)<u>laws and regulations</u> and independent judiciary system protect the private property right of businesses, thus reducing investment risks</li> </ul>	<ul style="list-style-type: none"> <li>• Uphold the (42)<u>rule of law</u> and independent judiciary system, which protects businesses' private property right</li> </ul>
<p><b>Physical</b></p>	<ul style="list-style-type: none"> <li>• A place with abundant natural resources attract foreign businesses</li> <li>• Good (43)<u>geographical location</u> fosters the development of import and export trade</li> </ul>	<ul style="list-style-type: none"> <li>• Hong Kong lacks natural resources, but she has a natural deep water harbour</li> <li>• Hong Kong is situated at the southern coast of the Mainland, which facilitates the re-export trade</li> </ul>
<p><b>Technological</b></p>	<ul style="list-style-type: none"> <li>• Well-established telecommunications network helps businesses communicate with the branches in other places and shortens the time of communication</li> <li>• Advanced technology increases the productivity of businesses</li> </ul>	<ul style="list-style-type: none"> <li>• Well-established (44)<u>broadband</u> networks facilitates the exchange of information</li> <li>• Businesses are more willing to invest in research and development</li> </ul>

<p><b>Socio-cultural</b></p>	<ul style="list-style-type: none"> <li>• Population (45)<u>size</u>, (46)<u>structure</u> and (47)<u>education level</u> affect the supply and quality of labour</li> <li>• Religions, lifestyles and social values affect the consumption patterns of the public</li> </ul>	<ul style="list-style-type: none"> <li>• Compulsory education raises the average education level of the population. It supports the development of tertiary production</li> <li>• (48)<u>Ageing</u> population may result in the shortage of labour in the future</li> <li>• Hong Kong is a multicultural society. Businesses can explore opportunities by opening niche markets</li> </ul>
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