

1. **Issues faced by businesses in Hong Kong**

- Increasing prices and rentals for commercial premises
- High labour costs

- **High operating cost:** Rent and wage level of Hong Kong is too high that investors are reluctant to start their business here.
- **Serious air pollution:** Air pollution will harm health and investors may withdraw their investment plan.
- **Stagnant technology development:** Inclination to service industry of Hong Kong leads to lacking resources in technological development. Investors would change to other places for their scientific research.
- **Lack of technical experts:** Hong Kong may lack those high technology experts involved in research
- **Over-reliance on imported food and raw material:** Primary production in Hong Kong is scarce and price soar of imported food and raw material will cause imported inflation.

2. **Methods to solve the high costs in HK**

- employing more **part-time staff** so as to save costs on salaries and fringe benefits
- moving to a district in Hong Kong with lower rents, e.g remote area
- **contracting out** some jobs on a **project basis to freelancers** so that the bank can rent less office space

3. **The major factors accounting for the structural changes to tertiary sectors include:**

- China adopted its **open-door policy** in 1978 which encouraged foreign investments.
- Many Hong Kong manufacturers **relocated** their factories to the Mainland to lower their production costs.
- There was a growing demand for **high value-added services** (e.g., finance, banking, IT, marketing, design) to support relocated factories.
- Hong Kong has become a **financial and service centre** to support business activities (e.g., trading, tourism, investment) on the Mainland.
- Hong Kong is transforming itself into a **knowledge-based economy**.

4. Business sector contribute to the Hong Kong economy in the following ways.

- **Providing employment opportunities:** The business sector promotes Hong Kong's economic growth and provides employment opportunities for Hong Kong's labour force.
- **Producing income:** The business sector enables the people of Hong Kong to earn an income and raise their living standards.

- **Earning foreign exchange to pay for imports:** The business sector enables Hong Kong to earn foreign exchange to pay for its imports.
- **Serving the Mainland:** As one of the world's major financial centres, Hong Kong helps many Mainland enterprises raise capital and manage their assets.

- **Raising government revenue:** As the business sector prospers, private enterprises earn more profits. Transactions in the property market and the stock market will also increase. As a result, government revenue from land sales, profits tax, and stamp duties on property and stock transactions will rise.

5. **HK government receive revenue from the following means**

- profits tax from business
- land sales
- stamp duties on property and stock transactions

A strong economy will lead to a growth in companies' earnings and business transactions. As private enterprises earn more profits, they will pay more profits tax to the government.

6. **Relationships between HK and the Mainland**

The Mainland is

- an important **market** for **Hong Kong's exports**,
- the largest source of Hong Kong's **imports and re-exports**.
- Hong Kong imports goods from other countries and **re-exports them to the Mainland**,
- HK imports goods from the Mainland and **re-exports them to other countries**.
- Hong Kong also imports a lot of **food and consumer goods** from the Mainland for its consumption.

Hong Kong is

- an important **service centre** for the Mainland.
- It provides a wide range of **financial and business services** to individuals and firms in the Mainland,
- such as *banking and finance, insurance, transport, accounting, tourism, marketing and sales promotion*.
- In return, enterprises in the Mainland also **facilitate** Hong Kong firms (e.g., property developers, sellers of consumer products) in **exploring and developing the Mainland market**.

7. Hong Kong serve as an **intermediary** between the Mainland and the outside world:

- Many Mainland enterprises **raise capital** by listing on Hong Kong's stock exchange.
- As a major financial centre in the world, Hong Kong helps the Mainland enterprises raise capital and manage their assets.
- Hong Kong serves as an **entrepôt** for trade between the Mainland and the outside world.
- Hong Kong enterprises **import technology and knowledge** to China while setting up production bases in China.
- Hong Kong is often regarded as a **stepping-stone** to the Mainland market.
- Hong Kong provides **many financial and business services** to firms in the Mainland, e.g., banking and finance, insurance, transport, accounting, marketing and sales promotion. This helps Mainland enterprises do business with overseas enterprises.

8. **Political instability is bad for business:**

(such as wars, religious conflicts, social unrest), the Middle East is the riskiest region for investment.

• Political and legal factors: labour law, environmental protection law, customs rules, etc.
e.g. whether the local government has favourable policies towards the IT industry

- The Hong Kong government maintains **open and fair competition** in the market.
- The Hong Kong government allows the **free flow of information**.
- Hong Kong **respects private property rights** and **upholds** the rule of law.
- Hong Kong has set up the **ICAC** to prevent corruption and bribery.

9. The '**Individual Visit Scheme**' implemented in 2003 promotes tourism in Hong Kong and makes industries such as hotel, catering, retail and transportation more vibrant.

The implementation of **Closer Economic Partnership Arrangement (CEPA)** strengthens the cooperation between mainland China and Hong Kong on trade and investment and prompts mutual development.

- CEPA **opens up huge markets** for Hong Kong goods and services
- CEPA **helps Hong Kong attract foreign direct investment**
- **Zero tariffs:** Those products manufactured in Hong Kong (e.g. Textile) can enjoy zero tariffs through CEPA and some factories plan to move the value added process back to Hong Kong.
- **Recognition of professional qualification:** Several professionals (e.g. Auditing) can be recognized a portion of their professional qualifications so that it is more appealing for professionals to develop their career in China.

10. **Favorable factors which enable HK to become 'Asian regional headquarters'**

- HK adopts a **free trade policy** with little government intervention.
- HK allows the **free flow of capital** and has **no foreign exchange controls**.
- As the Hong Kong dollar is pegged to the US dollar, Hong Kong has a **stable exchange rate**.
- Global network (transport and communication): quick access to information and timely delivery of news
- Skillful and productive workforce: high quality and more professional
- **maintaining law and order.** For example, Hong Kong Police Force maintains public order so that Hong Kong is regarded as a safe city for investments.
- providing **education and training** to Hong Kong people in order to improve their productivity and competitiveness. For example, workers in Hong Kong can further their study in local tertiary institutions.
- All of these allow business to **freely transfer capital** in and out of the territory.
- HK has a **favorable location** (near the Mainland). This helps many companies expand its business to cities in the Mainland.
- Hong Kong has **advanced information and communication technology** to support trading in the financial market.
- Hong Kong can help Mainland enterprises **raise capital** with its sophisticated financial system.
- It has a well-developed **infrastructure** (roads and ports).
- A **simple tax system and low tax rate** also attract foreign investment.

11. • **Economic factors:** wage level, price level (affecting rent and other production costs), control of capital inflows and outflows, taxation policy, etc.
e.g. whether there is sufficient space for expansion at reasonable cost

The **income level** of Hong Kong consumers is high relative to other Asian countries or Mainland cities. Hong Kong people can afford lots of products which target higher-income earners.

12. **Six industries in HK** include:

educational services, medical services, environmental industries, innovation and industry, cultural and creative industries and testing and certification services.

13. • **Social and cultural factors:**

population structure (affecting labour supply), education levels and language ability of the population (affecting labour productivity), etc.

e.g. whether there is an adequate supply of programming workers

Hong Kong is now facing the **problem of ageing population**. It is an unfavourable social factor for Hong Kong's business environment.

Ageing population means that the proportion of young workers decreases and the proportion of elder workers increases. This will lead to a decrease in labour supply of Hong Kong.

As the workforce in Hong Kong consists of more and more elderly workers, the **labour productivity** of Hong Kong will also decrease.

14. A **laissez-faire** economic policy is

- based on the idea that the government should minimise its intervention in the market.
- The allocation of resources is to be determined by market forces.
- Hong Kong is regarded as a free market economy with little government intervention.
- It promotes a free market and free trade.
- For example, anyone can start a business in Hong Kong and people can exchange goods and services freely in the market.

15. **In Hong Kong, the government allows the free flow of information.**

- The media enjoy a high degree of freedom.
- Firms can quickly obtain information about changes in the business environment which is useful for making timely business decisions.
- All of these help Hong Kong become and remain a global centre for trade, finance, business and communications.

16. Hong Kong is regarded as an **externally-oriented economy** because

- it relies heavily on external trade and foreign investment.
- Volatility in the global economy can cause a surge or drop in the demand for Hong Kong's goods and services, with external trade and foreign investment directly affected as a result.

Hong Kong relies heavily on external trade because:

- Hong Kong lacks natural resources and arable land. It needs to import foodstuffs and fuel from the Mainland and other countries.
- Hong Kong depends on other countries to supply consumer durables, such as automobiles, televisions and machines.
- As an entrepôt, Hong Kong imports many goods from the Mainland and other countries and re-exports these goods to other countries and the Mainland.

17. **Technology** transfers from other countries can *improve production techniques and labour productivity* of Hong Kong firms. This helps reduce their production costs.

Technology transfers help *improve the knowledge and skills of workers* in Hong Kong. Their *income* increases as a result. They can thus enjoy a *higher standard of living*.

Advances in information and communication technology and transport technology have lowered *communications and transport costs*.

It has become more **economical to transport raw materials and products** around the world. This allows firms in Hong Kong to save on production costs by outsourcing their production processes.

Technology **promotes the widespread use of the Internet** which has greatly improved information flows. For example, Hong Kong firms can obtain information on the Internet to buy inputs from the lowest-cost suppliers throughout the world. This can greatly lower the production costs.

The wider use of technology can also facilitate Hong Kong in its transformation into a *knowledge-based economy*.

- Technological factors: ICT and transport technology (affecting communications and transports costs), etc.

18. **Technological** factors can help raise the **productivity** of a bank in the following ways:

- **Cloud computing** enables the bank to store data on servers at a remote location. The bank can thus save and backup a lot of data at a lower cost. Employees at the bank can also work at home. Employees with minor health problems who are taking sick leave can work remotely at home.
- The bank can develop **new ATM machines** which can process transactions faster. For example, some banks are developing **mobile applications** which enable customers to take money from ATM machines without a bank card. Customers are first required to input personal data and transaction details via their smartphone. A verification code will then be sent to the customers. They can then input the code at ATM machines to get the money.
- The bank can develop **online banking (Internet banking)** which allows customers to conduct transactions on a secured website. This can speed up banking transactions. Alternatively, the bank can set up a self-help personal banking centre which encourages customers to take part in the transaction process. The bank can thus hire fewer tellers at its branches.

19. **Multi-National Companies**, like McDonalds

- An **MNC** can produce and sell its products at different locations around the world.
- It can reduce its business risks by diversifying its business operations and markets.
- Thus, the MNC would not be seriously affected by labour strikes and demand fluctuations in a single country.

20. The reasons that *MNCs set up businesses in Hong Kong* are as follows:

- Hong Kong provides a **stable political environment and a sound legal system**.
- Hong Kong has a **simple tax system and its low tax rate** can attract foreign investments.
- Hong Kong allows a **free flow of information**. This allows investors to obtain the latest information about changes in the global market.
- Hong Kong has a **favourable location (near the Mainland)**. This attracts foreign companies which want to enter the Mainland market to set up businesses in Hong Kong.
- The Hong Kong government pursues a **laissez-faire policy**, which promotes the **free market and free trade**. Except for certain industries, such as public transport services, any foreign investor can start a business in Hong Kong. The possibility of government intervention in their business is low.
- The Hong Kong government does **not impose any trade barriers**, such as tariffs or quotas on imported goods. MNCs can export goods to Hong Kong without paying any tariffs.
- There are **no foreign exchange controls**. The Hong Kong government does not control capital inflow and outflow. MNCs can freely move their capital in and out of Hong Kong. They can make use of their capital to explore investment opportunities.

21. **Issues to be considered when hiring staff / company from other countries**

Is/can the staff or the company:

- **suitable** to provide the kinds of services needed
- provide **quality** services? IT support services and customer services
- have good **work ethics** (i.e., will the employees steal the client information from the company?)
- **the cost of outsourcing** justifiable
- whether **customers are satisfied** with the services provided by the other company
- whether **internal employees can communicate effectively** with the employees from the other company
- **monitor the service quality** of the other company on an ongoing basis
- **Business and Cultural differences**

22. **Outsourcing** is the act of a company contracting out a production process or a business function to another company within or outside the country.

Firms outsourcing production and customer service to other low-cost countries can **lower their costs**.

Since the firms do not own the facility, it gives them more flexibility to adjust their production plan.

Major issues and concerns that MNCs need to be aware of include differences in *business cultures and practices, work ethics, product quality control systems*, etc., between the MNC and the outsourcing company.

If the products made or services provided by the outsourcing company are of *poor quality*, or if the outsourcing company pollutes the environment, the *reputation* of the MNC will be harmed.

To address the issues and concerns in part (c), MNCs should:

- **monitor** the quality of products and services produced by outsourcing companies on a continuous basis.
- help outsourcing companies **train** their workers and **establish** a good **quality control system**.
- request that outsourcing companies follow their **codes of conduct** or good practices.

23. • **Physical factors:** favourable location, proximity to infrastructure (roads and ports), transportation network, availability of natural resources, etc.

Benefits arising from the favourable physical factor of having a natural deep-water harbour:

- The natural deep-water harbour provides a **port** for large ships, linking Hong Kong to the world.
- The natural *deep-water harbour* helps promote the growth of the **freight industry** in Hong Kong.

Benefits arising from the favourable physical factor of its **proximity to the Mainland:**

- Due to its proximity to the Mainland, Hong Kong serves as a vital intermediary between the Mainland and the outside world.
- Hong Kong earns foreign exchange by providing services to facilitate trades between the Mainland and other countries.
- Viewing Hong Kong as a stepping stone to the Mainland market, many foreign firms have set up headquarters and offices in Hong Kong.
- Hong Kong's financial sector prospers as it helps many Mainland firms raise capital in the stock market.
- Hong Kong is easily accessible to Mainland people due to its proximity to the Mainland. Residents of some Mainland cities can also travel to Hong Kong easily under the Individual Visit Scheme. This helps promote the development of Hong Kong's tourism.
- Good transportation network links Hong Kong to the Mainland. Hong Kong businesses can set up factories in the Mainland to save on production cost.

24. **Costs of relocating plants to China:**

- Relocating production plants to other countries in Asia involves high set-up costs. The company has to build new plants and recruit new workers.
- It takes time to train new workers.
- The company may find it difficult to monitor and control production plants in different countries.
- Many countries in Asia are politically unstable. The safety of workers and production plants may be threatened.
- The company may not be familiar with the business environment in other countries.

Benefits of relocating plants to China:

- Production costs may be lowered by relocating plants to other low-cost countries in Asia.
- The governments of these countries may adopt favourable policies to attract foreign investment in manufacturing industries. This will enhance the competitiveness of the company.
- Business risks can be diversified by carrying out production in different countries.
- As part of the process of relocation, the company can explore new markets in other countries.
- The image of the company can be enhanced by establishing production plants in different countries.

25. **Globalisation** affects business decisions in the following ways:

- Firms can utilise the **Internet** to *explore new markets* in other countries and to sell their products to *foreign buyers*.
- Firms can make good use of **capital** to *explore business opportunities worldwide*.
- They can **diversify their investment** around the world (e.g., by setting up production bases and businesses overseas) to reduce their risks.
- Firms can **raise capital** in other countries (by borrowing from overseas banks and listing on foreign stock markets) for business expansion.
- Firms can **specialise** in the production of goods and services in which they have a comparative advantage and export them to other countries.
- Firms can buy inputs from the **lowest-cost suppliers** throughout the world (i.e., global sourcing).
- Firms can **outsource production processes** in which they do not have a comparative advantage to foreign firms.

26. **Globalisation** is a series of economic, technological, cultural, social and political changes which have led to the increasing integration and interdependence of people and firms around the world.

In the age of globalisation, many firms have expanded their market overseas and global competition has become more intense.

Hong Kong business firms not only face competition in the local market, but also face competition from foreign firms in overseas markets.

Under globalisation, there is a greater mobility of factors of production (e.g., capital and labour) between countries.

Hong Kong business firms need to compete with foreign firms for capital and talent.

27. A small manufacturer in Hong Kong can better respond to global competition by:

- developing its own brand names to differentiate its products from competitors.
- setting up joint ventures with foreign companies to increase their competitiveness.
- specialising in the production of goods in which they have a comparative advantage and exporting them to other countries.
- expanding its businesses to other countries to make its brand or company international.