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Economic report: Hong Kong 2009 Update

1. Appreciation of the economic problems and issues

1.1 General overview of HK's economy: The Hong Kong economy rebounded in the second quarter of 2009, benefiting from the faster growth of the Mainland economy and the waning of recessionary forces in the advanced economies. Following a sharp year-on-year contraction of 7.8% in the first quarter of 2009, real GDP registered a smaller decline of 3.8% in the second quarter. On a quarter-to-quarter comparison, the economy resumed growth at 3.3% in the second quarter, ending the contraction in the previous four quarters. The HKSAR Government has just revised its forecast of GDP for 2009 to contract by 3.5-4.5%, up from the forecast decline of 5.5-6.5% in May 2009.

Total exports of goods declined by 12% year-on-year in the second quarter of 2009, much smaller than the 23% decline in the first quarter. On a quarter-to-quarter comparison, total exports of goods rebounded strongly by 12% in the second quarter of 2009. The relative improvement was most evident in exports to the Mainland market, and to a lesser extent in some other Asian markets. However, the performance of the US and EU markets still lagged behind others. Likewise, imports of goods contracted at a smaller rate of 12% year-on-year in the second quarter of 2009, as compared to the 22% decrease in the first quarter. On a quarter-to-quarter comparison, imports of goods rose by 12% in the second quarter of 2009.

Private consumption expenditure rebounded by 4.0% in the second quarter over the first quarter, leading to a much lesser year-on-year decline of 1.0% than the 6.0% decline in the first quarter. However, business sentiments remained cautious. Fixed investment fell by 14% in both the first and second quarters over a year earlier.

There are mixed messages in unemployment rate. On one hand, it reached 5.4% in April-June 2009. On the other hand, the pace of increase in unemployment rate began to slow down.

The monetary and financial systems of Hong Kong remain resilient when compared with the US and Europe. The exchange rate with the US dollar, under the dollar peg, is stable. The capital adequacy ratio of the Hong Kong banking institutions is high while asset quality of the local banking sector is rather sound. The default ratio for residential mortgage loans was steady at 0.05% in Jan-June 2009.

Although the economy of Hong Kong rebounded in the second quarter, the economic outlook remains uncertain. For a small and open economy like Hong Kong, a sustained and solid recovery will hinge on a visible improvement in the external environment.

1.2 Measures adopted by the HKSAR Government in response to the financial crisis: To stabilize the financial market, the HKSAR Government uses the Exchange Fund (reserve backing the Hong Kong dollar) to provide full deposit protection.

To boost the real economy, the HKSAR Government will expedite infrastructure projects, create more jobs, provide export credit insurance and provide loan guarantees for enterprises. As at end-July 2009, the government has approved loans of about US$ 4.68 billion benefiting some 11,000 firms which employ over 190,000 employees.

According to the HKSAR Government, the discretionary relief measures amounted to about US$ 11.2 billion or 5.2% of GDP. The measures taken would raise GDP by about 2% in 2009.

1.3 Development of six economic pillars: Chief Executive Donald Tsang established the Task Force on Economic Challenges in response to the global financial crisis. After the last meeting of the task force in June 2009, the HKSAR Government announced to develop six economic pillars for the medium and long-term growth of the Hong Kong economy. These six sectors are educational services, medical services, testing and certification, environmental industry, innovation and technology as well as cultural and creative industries.

i) Education services: The government will provide suitable sites within the urban area to support the development of self-financed post secondary and higher education programmes by interested sponsoring bodies. It will review the Post-Secondary Colleges Ordinance (Cap. 320) to provide a legal framework to facilitate the development of self-financed post secondary and higher education institutions with potential and capabilities.

ii) Medical services: The government will reserve suitable sites for auction by operators interested in providing private medical services. It will speed up the establishment of the medical centres of excellence in paediatrics and neuroscience to further promote public-private partnership. In addition, the government will enhance training of medical professionals and create favourable conditions to attract more medical talents from outside Hong Kong for exchange of expertise, research and training.

iii) Testing and certification: A “Hong Kong Council for Testing and Certification” will be established to enhance professional standards and recognition of testing industry in the international arena, and explore more business opportunities. The government will continue to provide more business opportunities for private laboratories, for example, by increasing outsourcing of food tests to complement new legislation, and encourage the Chinese medicine trade to monitor the quality of Chinese medicine products by conducting basic tests on their products on a regular basis. The government will promote testing and certification services of Hong Kong in the Mainland and overseas. Also, it will pursue discussions with the Mainland authorities to seek their agreement to recognise the testing reports of Hong Kong-accredited laboratories.

iv) Environmental industry: The government will set a good example by expanding the scope of green procurement and will support the recycling industry. It will launch a pilot recycling scheme at the EcoPark by inviting non-profit making organizations to participate in the collection and processing of recyclables such as waste plastics and waste electrical and electronic equipment.

v) Innovation and technology: The government will actively explore the provision of financial and policy incentives to encourage more R&D investment in the private sector. It will provide more resources to the five R&D Centres to roll out more applied R&D projects and to strengthen their work in commercialization.

vi) Cultural and creative industries: The government will consider policy initiatives to facilitate the conversion or redevelopment of under-utilised industrial buildings to provide more useable floor space and land for the cultural and creative industries. It will also organise more major regional events which can be further expanded to become signature events such as the Entertainment Expo and the Business of Design Week for creative industries in the region.

How the promotion of these fields in Hong Kong may bring business opportunities to Swiss companies will be discussed in 3.2.3 “Outlook for Swiss exports to Hong Kong”

1.4 Economic integration with Mainland China: Hong Kong's trade with China is to a large extent related to outward processing activities. More than 80% of Hong Kong manufacturers have established production facilities in China. In Jan-June 2009, Hong Kong’s domestic exports were confined to about 2.4% of its total exports while re-exports accounted for about 97.6% of its total exports. Hong Kong is the most important entrepôt for China. If re-exports to and from China are included, about 17% of China’s foreign trade is handled via Hong Kong.

Hong Kong is the largest source of overseas direct investment in China. By the end of 2008, among all the overseas-funded projects registered in China, 45% were tied to Hong Kong interests. The stock of utilized capital inflow from Hong Kong amounted to about USD 350 billion, accounting for 40% of the national total. On the other hand, China is the biggest investor in Hong Kong. According to the HK Census and Statistics Department, China’s cumulative direct investment in Hong Kong was USD 479 billion or 41% of Hong Kong's total stock of inward direct investment at the end of 2007.

Hong Kong is a key offshore capital-raising centre for Chinese enterprises. As of June 2009, total market capitalization of China-related stocks in the Main Board reached 943 billion or 52% of the market total. In the past 10 years, mainland companies have raised more than USD 180 billion in Hong Kong.

For information on the Closer Economic Partnership Arrangement (CEPA) and Pan-Pearl River Delta (PPRD) Cooperation, please refer to 2.2 and 2.3

1.5 Situation of HK enterprises in the Pearl River Delta PRD: According to the Hong Kong Trade Development Council (HKTDC), there are about 57,500 HK-funded factories in the PRD. In a move to upgrade the processing trade and to contain the production activities of "high energy consumption, high pollution and resource consumption" industries, China tightens its control of the processing trade and adjusts relevant regulations. The Guiding Opinions on Promoting Industrial Relocation and Cooperation in the Pan PRD Region, published by the Guangdong Development and Reform Committee, confirms Guangdong's pursuit of orderly relocation of Pan PRD industries. Those Hong Kong companies failing to upgrade their quality and technology will either be relocated to remote regions or be eliminated.

The Chinese Government has introduced some relief measures such as raising the VAT tax rebate rates and provision of loan guarantees for enterprises including those coming from Hong Kong, Macao and Taiwan.

In order to ease the negative impacts of the decline in exports, the Guangdong Government considers to help enterprises in Guangdong to launch domestic sales. The Guangdong Government has contacted the governments of Hong Kong and Macao with plans to organize two to three major sales promotional events in the Northern part of China as well as to participate in various exhibitions in China to open up the domestic market.

According to a survey conducted by the Federation of Hong Kong Industries FHKI in Feb-April 2009, the biggest problem for Hong Kong enterprises in the PRD since the outburst of global financial crisis was shrinking orders. Other major difficulties included dwindling of profit margins, rising operation costs, high payment default and tightening of credit lines by banks. The enterprises adopted some coping strategies such as cutting down production capacity, adjusting investment plans and searching for new orders in domestic (Mainland China) and emerging markets. Their sentiments were in general pessimistic. The FHKI made a supplementary survey in May 2009 and found that the participating companies were more optimistic when compared with the survey results in Feb-April. The participating companies felt that the economy showed some signs of slight improvement. The companies saw gradual increase in orders and would cease to lay off staff.

1.6 US Dollar peg: The Linked Exchange Rate System (HK$7.8: US$1) has been introduced to stabilize the then volatile economy and financial market since 17th October 1983. Norman Chan, the newly appointed chief executive of the Hong Kong Monetary Authority, reaffirmed in July 2009 to maintain the dollar peg. He mentioned that the dollar peg was the foundation of the monetary and financial stability of Hong Kong.

1.7 Pilot RMB Trade Settlement Scheme: The Chinese Government announced in April 2009 the scheme of allowing settlement in Renminbi (RMB) in the trade of Shanghai, Shenzhen, Guangzhou, Zhuhai and Dongguan with Hong Kong and Macao. The People's Bank of China and the Hong Kong Monetary Authority signed a memorandum of understanding in June 2009. This scheme would boost Hong Kong to become a RMB offshore centre and consolidate its status as an international financial platform. As far as China is concerned, it is a small but important step for the internationalization of the RMB in the future. For Hong Kong companies with manufacturing units in China, this scheme could provide more flexibility in their operations and help them to reduce their exchange risks as well as lowering their costs.

2. International and regional economic agreements
2.1 HK's policy and priorities

Hong Kong is a free port which thrives on free trade. Its open door policy has enabled the city to become the world's 13th largest trading economy and an international financial and commercial centre serving the Asia-Pacific region and China. The cornerstone of this approach is a strong and credible multilateral trading system.

Hong Kong is a founding member of the World Trade Organization (WTO). Hong Kong became a member of the Asia-Pacific Economic Cooperation (APEC) and the Pacific Economic Cooperation Council (PECC) in 1991. Hong Kong belongs, in its own right, to the Asian Development Bank (ADB) and the World Customs Organization (WCO). Since April 1994, Hong Kong has been an observer in the Trade Committee of the Organization for Economic Cooperation and Development (OECD).

Hong Kong has so far concluded one free trade agreement, that is, the Closer Economic Partnership Arrangement (CEPA) with Mainland China. Details as per 2.2. At present, Hong Kong is negotiating with New Zealand for a bilateral free trade agreement.

Furthermore, Hong Kong has signed investment promotion and protection agreements with 16 countries including Finland, the Netherlands, Australia, Denmark, Sweden, **Switzerland**, New Zealand, Italy, France, Germany, Belgo-Luxembourg Economic Union, Austria, Japan, Korea, the United Kingdom and Thailand.

2.2 Closer Economic Partnership Arrangement (CEPA)

The Closer Economic Partnership Arrangement (CEPA) is the first ever regional trade agreement signed between China and Hong Kong. It was signed in 2003 and came into effect from Jan. 2004. It covered 3 broad areas, namely 1) trade in goods, 2) trade in services and 3) trade and investment facilitation. As a living agreement, the scope of market access and liberalization measures have been expanded progressively under CEPA II – V in subsequent years.

At present, all products of Hong Kong origin, except for a few prohibited articles, can be imported into the mainland tariff free under CEPA. Since the tertiary sector accounts for more than 90% of GDP in Hong Kong, the real significance of the CEPA lies in the trade in services.

China and Hong Kong signed CEPA VI covering further services liberalization measures on 9th May 2009. The measures will take effect from 1st October 2009.

Further services liberalization under CEPA VI

Under CEPA VI, the Mainland will introduce 29 liberalisation measures covering 20 services sectors, including 2 new sectors (rail transport and research & development). The total number of service sectors covered by CEPA will be expanded from 40 to 42[1]. Among them, the noteworthy liberalisation measures are:

On tourism, Mainland travel agents authorised to operate group tours to Taiwan can organise group tours for Mainland residents, who hold a valid exit/entry permit for travelling to and from Taiwan and travel endorsement, to enter and remain in Hong Kong in transit. This measure aims to facilitate the travel trade in the Mainland and Hong Kong to develop multi-destination tour products.

[1] It includes legal services, accounting, construction and real estate, medical and dental, advertising, management consulting, convention and exhibition, telecommunications, audiovisual, distribution, insurance, banking, securities and futures, tourism, transport, freight forwarding agency, storage and warehousing, logistics, air transport, information technology, professionals qualification examinations, cultural and recreational, trade mark agencies, patent agencies, job referral agencies, job intermediaries, individually owned stores, computer and the related services, market research, management consulting services, public utility, building-cleaning, photographic, printing, translation, environmental, social services, sporting, mining services, scientific and technical consulting, rail transport and research and development.

On banking, branches established by a Hong Kong bank in Guangdong Province can set up "cross-location" sub-branches within Guangdong Province. It will enable the banks to expand their business network, and improve the quality and efficiency of banking services provided to enterprises (including Hong Kong-invested enterprises in Guangdong Province).

On securities services, qualified Hong Kong securities companies and Mainland securities companies can set up in Guangdong Province joint venture securities investment advisory companies, with the scope of business focusing specifically on securities investment advisory services. The percentage of shareholding of the Hong Kong securities company could, at a maximum, reach 1/3 of the total shareholding of such a joint venture securities investment advisory company. This will allow Hong Kong securities companies to participate in the development of the Mainland's securities market.

On audio-visual services, Hong Kong service suppliers (HKSS) can provide videos and sound recording (including motion picture products) distribution services on the Mainland in the form of wholly-owned operations.

On telecommunications services, HKSS can distribute in Guangdong Province fixed/mobile telephone service cards which can only be used in Hong Kong.

In relation to legal services, the Mainland will allow Hong Kong legal practitioners who have at least five years' experience in legal practice and who have passed the National Judicial Examination to undergo intensive training offered by lawyers associations on the Mainland. Upon completion of the training and passing of the assessment, they can apply to practise as lawyers on the Mainland. Moreover, the Mainland will also allow Hong Kong law firms which have set up representative offices on the Mainland to operate in association with Mainland law firms in Guangdong Province.

On convention and exhibition, HKSS can organise exhibitions, in the form of cross-border supply, in Beijing Municipality, Tianjin Municipality, Chongqing Municipality, Zhejiang Province, Jiangsu Province and Fujian Province on a pilot basis. Furthermore, enterprises set up by HKSS on a wholly-owned, equity joint venture or contractual joint venture basis in the provinces and autonomous regions of Guangxi, Hunan, Hainan, Fujian, Jiangxi, Yunnan, Guizhou and Sichuan can organise overseas exhibitions on a pilot basis.

On transportation services, HKSS can construct, operate and manage the Shenzhen Metro Line 4 project in Shenzhen in the form of wholly-owned operations. It is a newly added service sector. In addition, HKSS can set up wholly-owned shipping companies on the Mainland to provide regular business services for the shipping transport between Hong Kong and Class B ports in Guangdong.

On printing and publishing services, HKSS can establish typesetting and production services companies on a wholly-owned, equity joint venture or contractual joint venture basis on the Mainland to provide pre-press services such as proof-reading, design and typesetting for books.

Regarding research and development services, which is also a newly added sector, HKSS can set up wholly-owned enterprises on the Mainland to provide research and experimental development services in the natural sciences and engineering.

Financial co-operation and mutual recognition of professional qualifications

Apart from service liberalisation, the two sides have also agreed to enhance financial co-operation and take forward the work on mutual recognition of professional qualifications.

To enhance financial co-operation, qualified Mainland securities companies approved by the China Securities Regulatory Commission can set up subsidiaries in Hong Kong in accordance with the relevant requirements. Furthermore, the Mainland will also actively explore the introduction on the Mainland of “open-end index-tracking exchange-traded fund”, the portfolios of which are constituted by Hong Kong listed stocks.

Regarding mutual recognition of professional qualifications, Supplement VI to CEPA also includes a number of measures to encourage mutual recognition of professional qualifications as well as technical exchange work among professionals from the accounting, construction, real estate and printing sectors.

Economic Benefits

Out of 8.2 million Chinese tourists to Hong Kong in the first half of 2009, 4.6 million Chinese tourists (57% of total and 7.3% increase year-on-year basis) travelled under the individual visit scheme (IVS) which was introduced in CEPA. It is arguable that many Chinese tourists would still have travelled to Hong Kong even without the IVS. Nevertheless, the IVS facilitates people's flow, promotes cross-boundary understanding and tightens business contacts between the mainland and Hong Kong. As the benefits are intangible, they are difficult to measure and quantify.

CEPA offers a good platform for Hong Kong products and services to have an effective access to China even though they have to face intensifying competition from Chinese companies and multinational competitors.

The mainland has undergone rapid economic development over the past two decades. The tertiary industry is quite lagged behind the secondary industry. To achieve more balanced growth and to take the economic development to a higher level, the Chinese Government has acknowledged the need to strive for quality growth supported by an efficient services sector. The significant part of CEPA to the mainland lies with the intangible benefits, that is, the transfer of quality capital and management and professional skills to the mainland for its long term economic development.

Supplement VI to CEPA includes a total of 9 liberalization measures for early and pilot implementation in Guangdong Province, covering the legal, convention and exhibition, public utility, telecommunications, banking, securities, maritime transport and rail transport sectors. Such measures can enhance co-operation of the services industry between Guangdong and Hong Kong.

Outlook for Switzerland

According to the information in our possession, some Swiss companies in Hong Kong take advantage of CEPA and have been qualified as Hong Kong Service Suppliers under CEPA and operating their business in China.

A Swiss company, qualified as a Hong Kong Service Supplier under CEPA, mentioned that CEPA as a whole was "useful, positive and beneficial" to their business in China. However, CEPA was an agreement signed between the Central Government and HKSAR Government and its implementation depends on the co-operation of various provinces, municipalities, cities and local authorities. According to the interviewee company, it encountered problems such as bureaucracy, different legal system, sophisticated tax regime, unpredictable modification and different interpretation of rules and regulations at the early stage of their entry to China. After some years of practical experience and more openness of China in general, its operation is now much smoother than before. Currently, it has established two offices in China under the framework of CEPA.

2.3 Pan-Pearl River Delta (PPRD) Cooperation

The "Pan-Pearl River Delta (PPRD)[2] Regional Co-operation Framework Agreement" was signed in 2004. The PPRD regional governments agreed to strengthen cooperation in 10 areas – infrastructure, investment, business and trade, tourism, agriculture, labour, education and culture, information and technology, environmental protection, health and prevention of infectious disease.

The 5th PPRD Regional Co-operation and Development Forum took place in Nanning, Guangxi on 9th - 11th June 2009. The HKSAR Government wants to strengthen ties with the PPRD region. The government would organise business matching events and trade fairs, and disseminate information on Chinese consumer markets and access channels so as to assist the Hong Kong business community.

[2] The PPRD region, also known as "9+2", comprises nine provinces/regions including Fujian, Jiangxi, Hunan, Guangdong, Guangxi, Hainan, Sichuan, Guizhou and Yunnan, as well as Hong Kong and Macao Special Administrative Regions.

In view of the current adverse economic environment, Hong Kong would act as a bridge in PPRD regional co-operation to jointly overcome the economic crisis.

3. Foreign trade
3.1 Development and general outlook
3.1.1 Trade in goods

According to the HKTDC, Hong Kong is the world's 13th largest trading economy.

In Jan-June 2009, total exports of Hong Kong fell by 17% (year-on-year basis) and amounted to US$ 143 billion. Major export markets were China (50% of total exports), the US (12%), Japan (4.6%), Germany (3.5%) and UK (2.5%). Major export products were electrical machinery and apparatus (26%), telecom and AV equipment (16%), office machines and computers (10%), clothing (7.4%) and textiles (3.4%).

On the other hand, imports dropped to US$ 153 billion (-19% year-on-year basis). Major suppliers were China (46% of total imports), Japan (8.4%), Singapore (6.5%), Taiwan (6.3%) and the US (5.7%). Major import products were electrical machinery and apparatus (26%), telecom and AV equipment (13%), office machines and computers (9.3%), clothing (4.6%) and textiles (3.2%).

For details, please refer to Appendix 3a (2008) and Appendix 3b (Jan-June 2009).

Regulations: Hong Kong is a free port and there is no tariff on general imports except duty on liquors, tobacco, hydrocarbon oil and methyl alcohol.

There are no regulatory measures impinging on international trade other than those required to discharge international obligations or to protect health, environment and access to hi-technology.

3.1.2 Trade in services

Exports of service amounted to US$ 38 billion (-6% year-on-year basis) in the first half of 2009. It decreased by 5.7% in the second quarter of 2009 from a year earlier, compared with the 6.3% decrease in the first quarter. On a quarter-to-quarter comparison, exports of services grew by 1.2% in the second quarter. Exports of services included: transportation services (30% of total), trade-related services (28% of total), financial and other services (23% of total) as well as travel services (19% of total).

Imports of service dropped to US$ 19.6 billion (-7.6% year-on-year basis) in the first half of 2009. It fell by 5.6% in the second quarter of 2009 over a year earlier, after contracting by 9.6% in the preceding quarter. On a quarter-to-quarter comparison, exports of services grew by 1.8% in the second quarter. Imports of services consisted of travel services (38% of total), transportation services (30% of total), financial and other services (26% of total) as well as trade-related services (6% of total).

3.2 Bilateral trade with Switzerland
3.2.1 Trade in goods

According to the Hong Kong Census and Statistics Department (HKCSD), Switzerland was the 12th largest trading partner of Hong Kong in Jan-June 2009. Switzerland was Hong Kong's 11th largest supplier and 20th largest export market.

In the first half of 2009, Swiss exports to Hong Kong amounted to CHF 2.7 billion (decreased by 1.5%). Major Swiss exports included jewellery & precious metal[3] (44% of total, increased by 60%, CHF 1.2 billion in value), watches and clocks (38% of total, dropped by 22%, CHF 1 billion in value), chemical and pharmaceutical products (6.2% of total, dropped by 30%, CHF 167 million in value) and machinery (5.4% of total, dropped by 25%, CHF 146 million in value).

[3] Among others, the exports of platinum, palladium and rhodium (HS code 7110) alone reached CHF 861 million or 242% increase year-on-year basis.

At first glance, Swiss exports to Hong Kong recorded only a moderate drop. However, the figures are distorted by a sharp increase in exports of a single commodity (please see footnote 3). In fact, all major export products such as watches and clocks, chemical and pharmaceutical products as well as machinery marked a fall between 22% and 30%.

In Jan-June 2009, China (including Hong Kong) maintained the status as the biggest market for Swiss products in Asia (5.7% of global Swiss exports), whereas China and Hong Kong accounted for 2.7% and 3% respectively.

In the first half of 2009, Hong Kong exports to Switzerland dropped by 34% to CHF 498 million. Major products included jewellery & precious metal (48% of total, dropped by 49%, CHF 240 million in value), watches and clocks (28% of total, increased by 2.6%, CHF 141 million in value), machinery (12% of total, decreased by 19%, CHF 59 million in value) and textiles and garments (2.8% of total, dropped by 37%, CHF 14 million in value).

As far as the bilateral trade in goods between Switzerland and Hong Kong is concerned, Switzerland got a trade surplus worth CHF 2.2 billion in the first half of 2009.

According to the HKCSD, Swiss exports to Hong Kong totalled USD 2,543 million (-5.9%) in Jan-June 2009 of which goods worth US$ 754 million were re-exported to other countries and notably to China. Swiss goods worth US$ 318 million (dropped by 21%) were re-exported to China via Hong Kong. Major products were watches and clocks (US$ 107 million), silver and platinum (US$ 22 million), measuring instruments (US$ 18 million), semi-conductors (US$ 16 million) and colouring matter (US$ 14 million).

There has been a notable growth for Swiss products entering China via Hong Kong in recent years (bar the first 6 months of 2009 due to the global economic downturn), from US$ 518 million in 2005, US$ 610 million in 2006, US$ 700 million in 2007 and US$ 867 million in 2008. In this regard, Swiss exporters and manufacturers may make use of Hong Kong as a known entrepôt and trade hub (which has a huge cluster of traders who are experienced in the market of China) to do business with China.

In the first half of 2009, products of Chinese origin worth US$ 511 million (dropped by 28%) were re-exported to Switzerland via Hong Kong. Major products were watches and clocks (US$ 223 million), clothing (64 million), jewellery (US$ 35 million) and telecom equipment (US$ 25 million).

3.2.2 Trade in services

According to the HKCSD, Hong Kong's exports of services to Switzerland amounted to US$ 1,056 million (1.3% of total exports of services, increased by 47%) in 2007[4]. Switzerland ranked 12th largest market for Hong Kong's exports of services. It consisted of transportation services (US$ 464 million), travel services (US$ 35 million), insurance services (US$ 5.8 million), financial services (US$ 93 million), trade-related services (US$ 235 million) and other services (US$ 223 million).

Hong Kong's imports of services from Switzerland reached to US$ 322 million (0.8% of total imports of services, increased by 19%) in 2007. Switzerland ranked 19th largest supplier in this category. It consisted of transportation services (US$ 66 million), travel services (US$ 39 million), insurance services (US$ 32 million), financial services (US$ 32 million), trade-related services (US$ 4.9 million) and other services (US$ 148 million).

3.2.3 Outlook for Swiss exports to Hong Kong

After four consecutive quarters of contraction, the economy of Hong Kong resumed growth at 3.3% in the second quarter of 2009. With the external environment showing a relative improvement, the exports of Hong Kong picked up and fared better than many other Asian economies in the second quarter of 2009. The improvement was most evident in exports to China (which accounts for about 46% and 50% of Hong Kong's imports and exports) while the performance of the US and EU markets still lagged behind.

[4] According to the HKCSD, the figures of the bilateral trade in services for 2008 will only be available by early 2010.

According to some industry sources, Chinese tourists account for about 70-80% of sales of Swiss hi-end watches in Hong Kong. In the sector of beauty products[5], Chinese tourists account for about 40-45% of their total sales in Hong Kong. However, despite a notable growth of Chinese tourists to Hong Kong in Jan-April 2009, the positive trend was reversed in May and June[6]. It is alerting if Chinese tourists continue to drop since they are a driving force of the retail market in Hong Kong, in particular for Swiss luxury and premium products. The Beijing Government agrees to expand the individual visit scheme (IVS) of mainland residents to Hong Kong. However, since these new visitors are either non-permanent Shenzhen residents (who can visit Hong Kong under the IVS by the end of 2009) or residents from remote cities and provinces, their consuming power may not be as high as those who travelled under earlier phases of the IVS.

In Jan-June 2009, exports of Swiss watches of high, medium and low price segments to Hong Kong recorded a decline of 21%, 32% and 5% respectively, according to the Federation of the Swiss Watch Industry Hong Kong Office. Since the global financial crisis, the middle class has been very prudent in their spending. The middle class is concerned with their job security and some of them have suffered loss in investment markets.

Thanks to the rebounds of both the stock market and the property market[7], local consumer sentiments improved in the second quarter. Private consumption expenditure rose by 4.0% in the second quarter over the first quarter. Better consumer confidence may help the sales of Swiss luxury and upscale products in the following quarters. When economic situation turns better, as what some analysts expect, the upper class will be more willing to spend on big-ticket items such as jewellery, watches, designer's fashion and valuable gifts. However, the products in demand have to be unique and prestigious. The world-renowned brands will therefore fare better.

Since the recovery of the global economy is still in the distance, capital investment from the private sector will remain weak. Demand for machinery and equipment is not going to revive soon.

As mentioned in 1.3, the government intends to promote the private health care sector. It will therefore offer business opportunities for Swiss medical services and apparatus. On the environmental industry, the government will lead to adopt green technologies in public projects. Swiss companies working in the environmental industry may seize business opportunities arising from large-scale development projects such as the West Kowloon Cultural District and Kai Tak cruise terminal project[8]. There will be good prospects for Swiss testing services and instruments due to increased customer awareness on food, drugs and consumer safety. The government wants to encourage more investments in R&D from the private sector through incentives. Details are yet to announce. It will be interesting to see if new incentives will change the mindset of local industrialists. If so, it will offer new opportunities to companies in high-technology sector and R&D institutions in Switzerland.

4. Direct Investments

4.1 Development and general outlook

According to the HKCSD, the stock of Hong Kong's inward direct investments was up by 59% to US$ 1,178 billion at the end of 2007[9]. Major investor countries were China (US$ 479 billion or 41% of total, grew by 84%), British Virgin Islands BVI (US$ 431 billion or 37% of total, grew by 72%), the Netherlands (US$ 68 billion or 5.8% of total, grew by 36%), Bermuda (US$ 49 billion or 4.2% of total, grew by 8.9%) and the US (US$ 36 billion, 3% of total, insignificant change in the stock).

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[5] Swiss beauty products imported to HK registered a growth of 32%, 19% and 23% in 2006, 2007 and 2008 respectively. However, it dropped by 22% in the first half of 2009 due to the economic downturn.

[6] Chinese tourists grew by 11% in Jan-April 2009 but dropped by 9.6% and 12% in May and June respectively.

[7] Hang Seng Index in Hong Kong rose to 31,638, an all-time high record, in October 2007 and dropped to 11,015 in October 2008. It was closed at 20,893 on 14th August 2009. According to the HKSAR Government, flat prices bounced up notably by an average of 14% between December 2008 and June 2009, with most of the gain occurring during the second quarter. The overall sale prices were only 5% below the high levels seen in mid-2008.

[8] The HKSAR government plans to create a cultural and entertainment hub in the West Kowloon, namely, the West Kowloon Cultural District. The first phase of the cultural district is due to be completed by 2015. Kai Tak cruise terminal will be built on the site of the former airport at Kai Tak. The first berth is expected to receive vessels by 2013.

[9] According to the HKCSD, the investment figures for 2008 will only be available by end December 2009.

China featured highly both as a destination for Hong Kong's outward direct investment (US$ 439 billion or 43% of total, ranked 2nd after BVI) and as the biggest source of HK's inward direct investment (as mentioned earlier). The substantial cross-boundary investment between China and Hong Kong reflected the close economic links between the two places.

The ratios of inward and outward direct investments were 568% and 488% of GDP respectively in 2007. It reflected Hong Kong as a highly externally oriented economy and an important business centre in the region with substantial cross-boundary investment. The highly ranked BVI and Bermuda reflected a common practice of Hong Kong and foreign enterprises in setting up non-operating companies in these offshore financial centres (known as tax haven economies) for channelling direct investment funds back to Hong Kong.

According to the International Monetary Fund (IMF), inward portfolio investments to Hong Kong reached US$ 782 billion (+35%) in 2007. Major investor countries were China (166 billion or 21% of total, grew by 68%), Cayman Islands (US$ 132 billion or 17% of total, grew by 71%), Bermuda (US$ 104 billion or 13% of total, grew by 63%), the UK (US$ 74 billion or 9.5% of total, grew by 2.8%) and the US (US$ 71 billion or 9% of total, grew by 9.2%).

In Hong Kong, there is neither restriction on inward and outward investments nor nationality restriction on corporate and sectorial ownership.

4.2 Bilateral investment flows

According to the HKCSD, Swiss direct investments in Hong Kong were about US$ 4.1 billion (0.4% of total, insignificant change in the stock) and ranked the 13th largest investor country in 2007[10] . Swiss portfolio investments in Hong Kong reached US$ 2.4 billion (0.3% of total, grew by 85%) and ranked 22nd investor country in 2007, according to the IMF.

As at 1st June 2008, 53 Swiss companies have set up their regional headquarters in Hong Kong. 63 Swiss companies have set up their regional offices whereas 63 Swiss companies have set up their local offices in Hong Kong. They are classified in various sectors: banking, beauty products, chemicals & pharmaceuticals, consultants, electronics, foodstuffs, freight forwarding, inspection, insurance, machinery/engineering, textiles & garments, watches/jewellery and trading houses, etc..

According to the HKCSD, the outward direct investments from Hong Kong to Switzerland for 2002, 2003 and 2004 were US$ 1.49 billion (ranked 14th), US$ 780 million (ranked 17th) and US$ 564 million (ranked 18th) respectively. The HKCSD compiles for top 20 recipient countries only. As Switzerland dropped out of this category in 2005-2007, the corresponding figure is no longer available.

5. Trade, economic and tourist promotion
5.1 Foreign economic promotion instruments

The Consulate General of Switzerland, the Federation Horlogère, Switzerland Tourism, the Swiss Chamber of Commerce in Hong Kong and the Swiss-Chinese Chamber of Commerce/the Swiss-Hong Kong Business Association are the organisations to promote Swiss economic interests in Hong Kong.

The Swiss Chamber of Commerce in Hong Kong

It is an organization with the mission to provide business platform and networking for Swiss companies and individuals in Hong Kong. It acts as an access to Greater China and Asia Pacific Region. For details, please visit its website www.swisschamhk.org.

Swiss-Chinese Chamber of Commerce/Swiss-Hong Kong Business Association

The Swiss-Chinese Chamber of Commerce is a non-profit association registered in Switzerland. Among their members are leading Swiss companies in the trade, industry and financial sectors. For details, please visit its website www.sccc.ch.

[10] According to the HKCSD, the bilateral investment figures for 2008 will only be available by end December 2009.

Switzerland Tourism

Despite a difficult economic climate and negative impact of the human swine flu against travel industry, Hong Kong visitors staying overnight increased by 2.9% to 29,038 in the first half of 2009. Switzerland Tourism organises a lot of activities to promote Switzerland in excellent image and top quality branding.

Fédération Horlogère

The Bienne based Federation of the Swiss Watch Industry (FH) is a private, professional and non-profit association which defends the watch industry's interests and contributes to its development. For details, please visit its website www.fhs.hk.

5.2 Interests for Switzerland as a location for investment, potential for development

Some Hong Kong companies have acquired Swiss watchmakers and producers of watch movements as a means to extend marketing and distribution network, and/or to gain access to better technology and designs. A noteworthy acquisition was the acquisition of Saia-Burgess by Johnson Electric, a Hong Kong company and one of the biggest manufacturers of micro motors in the world.

Apart from acquisitions, Switzerland as a location of research and development centres or international headquarters may be of interests to a limited number but well-established companies in Hong Kong.

5.3 Interests for Switzerland as a financial location, potential for development

A delegation of the Swiss Bankers Association visited Hong Kong to promote Swiss banking on annual basis in November 2008. The Consulate General of Switzerland organised their meetings/luncheon with media, Swiss banks, Swiss Chamber of Commerce in Hong Kong and senior officials of the HKSAR Government and relevant regulatory bodies.

6. Useful internet links

HK Government agencies:
HKSAR Government (http://www.gov.hk/)
Commerce and Economic Development Bureau (http://www.cedb.gov.hk/)
Trade and Industry Department (http://www.tid.gov.hk)
Census & Statistics Department (http://www.censtatd.gov.hk/)
Invest HK (http://www.investhk.gov.hk/)
Customs and Excise Department (http://www.customs.gov.hk)
HK Monetary Authority (http://www.info.gov.hk/hkma)
Office of the Commissioner of Insurance (http://www.oci.gov.hk/)
Intellectual Property Department (http://www.ipd.gov.hk/)

Swiss Government agencies and export promotion bodies
State Secretariat for Economic Affairs (http://www.seco.admin.ch/)
OSEC Business Network Switzerland (http://www.osec.ch/)

Statutory trade promotion bodies:
Hong Kong Trade Development Council (http://www.tdctrade.com)

Chambers and Associations:
Swiss Chamber of Commerce in HK (http://www.swisschamhk.org)
Swiss-Chinese Chamber of Commerce/Swiss-Hong Kong Business Association (http://www.sccc.ch/)
Swiss Association of Hong Kong (http://www.swiss-hk.com)
Federation of the Swiss Watch Industry, HK Office (http://www.fhs.hk)
HK General Chamber of Commerce (http://www.chamber.org.hk)
Federation of HK Industries (http://www.industryhk.org)
Chinese General Chamber of Commerce (http://www.cgcc.org.hk)
Chinese Manufacturers' Association (http://www.cma.org.hk)

Newspapers:
South China Morning Post (http://www.scmp.com)
The Standard (http://www.thestandard.com.hk)
Asian Wall Street Journal (http://www.wsj-asia.com)

Trade exhibitions calendar: (http://www.tdctrade.com/exh-con)

Appendices

1. Structure of the economy
2. Essential economic data
3a Trading partners 2008
3b Trading partners Jan-June 2009
4 Bilateral trade between Switzerland and Hong Kong
5. Main investor countries

<u>Appendix 1</u> **Structure of Economy**

	1995	**2006**	**2007**	**2008**	**% Change 1995 / 2007**
Spreading GDP (%)					
Primary Sector	0.2%	0.1%	0.1%.	n.a.*	-50%
Secondary Sector	16%	8.7%	7.7%	n.a.*	-52%
Tertiary Sector	83.8%	91.2%	92.3%	n.a.*	+10%
- Part of Public Services	n.a.*	n.a.*	n.a.*	n.a.*	n.a.*
Spreading Employment					
Primary Sector	0.6%	0.3%	0.2%	0.3%	-67%
Secondary Sector	27.1%	13.4%	13.2%	12.6%	-51%
Tertiary Sector	72.3%	86.3%	86.6%	87.1%	+20%
- Part of Public Services	n.a.*	n.a.*	n.a.*	n.a.*	n.a.*

n.a.* not available

Source: Hong Kong Census and Statistics Department

Appendix 2

Essential Economic Data

	2002	2003	2004	2005	2006	2007	2008	2009
GDP (USD billion)	159.9	158.5	165.8	177.3	189.1	207.1	215.2	207[a]
GDP per capita (USD)	23,466	23,150	24,100	26,000	27,600	29,900	30,800	29,600[a]
GDP growth (%)	1.9	3.2	8.6	7.1	7.0	6.4	2.5	-3.5 - -4.5[a]
Inflation (%)	-3.0	-2.6	-0.4	1.0	2.0	2.0	4.3	0.9[a]
Unemployment rate (%)	7.3	7.9	6.9	5.6	4.8	4.0	3.5	5.4[b]
Fiscal balance (% of GDP)	-4.8	-3.3	-0.3	1.0	4.0	7.2	-0.3	n.a.
Current account balance (% of GDP)	7.9	10.4	9.5	11.4	10.8	12.3	13.5	n.a.
Total external debt (% of GDP)	-	-	1	0.9	-	-	-	n.a.
Debt-service ratio (% of exports)	2.1	1.8	-	-	-	-	-	n.a.
Reserves (in months of imports)	22.6	23.3	21.1	19.8	18.6	19.5	22.3	n.a.

a government forecast for 2009
b April-June 2009
n.a. not available

Sources: HKSAR Government, IMF

Appendix 3a

Trading Partners 2008

	Exports to country/region	Exports (USD millions)	Share (%)	Growth* (%)
1	China	175,698	49	4.7
2	USA	46,058	13	-2.4
3	Japan	15,507	4.3	1.2
4	Germany	12,044	3.3	16
5	UK	9,665	2.7	0.7
6	Singapore	7,092	2	9.6
7	Taiwan	7,044	1.9	3.8
8	India	6,692	1.8	50
9	Korea Rep	6,354	1.8	-6.4
10	Netherlands	5,811	1.6	2
	EU	49,534	14	6.2
20	**Switzerland**	**2,659**	**0.7**	**47**
	Total	362,071	100	5.1
	Imports from country/region	**Imports (USD millions)**	**Share (%)**	**Growth* (%)**
1	China	180,863	47	6.1
2	Japan	38,148	9.8	3.6
3	Singapore	24,994	6.4	0.1
4	Taiwan	24,621	6.3	-6.4
5	USA	19,325	5	8.6
6	Korea Rep	15,139	3.9	-1.1
7	Malaysia	8,479	2.2	5.3
8	Thailand	8,174	2.1	11
9	India	7,438	1.9	22
10	Germany	6,851	1.8	11
	EU	29,291	7.6	12
12	**Switzerland**	**5,980**	**1.5**	**31**
	Total	387,857	100	5.5

* year-on-year basis

Sources : Hong Kong Census & Statistics Department, Hong Kong Trade Development Council

Appendix 3b

Trading Partners Jan-June 2009

	Exports to country/region	**Exports (USD millions)**	**Share (%)**	**Growth* (%)**
1	China	72,575	50	-14
2	USA	16,618	12	-21
3	Japan	6,363	4.6	-16
4	Germany	4,839	3.5	-13
5	UK	3,479	2.5	-21
6	India	3,131	2.2	-11
7	Taiwan	2,907	2	-15
8	Singapore	2,506	1.8	-31
9	Korea Rep	2,465	1.7	-26
10	Australia	2,149	1.5	-7.1
	EU	18,641	13	-20
20	**Switzerland**	**975**	**0.7**	**-34**
	Total	143,436	100	-17
	Imports from country/region	**Imports (USD millions)**	**Share (%)**	**Growth* (%)**
1	China	71,198	46	-16
2	Japan	12,848	8.4	-33
3	Singapore	9,905	6.5	-21
4	Taiwan	9,631	6.3	-23
5	USA	8,676	5.7	-9.6
6	Korea Rep	5,462	3.6	-29
7	Malaysia	4,031	2.6	-3.4
8	Thailand	3,175	2.1	-23
9	India	3,053	2	-23
10	Germany	2,780	1.8	-20
	EU	12,290	8	-16
11	**Switzerland**	**2,543**	**1.7**	**-5.9**
	Total	153,433	100	-19

* year-on-year basis

Sources : Hong Kong Census & Statistics Department, Hong Kong Trade Development Council

Appendix 4 Bilateral Trade Table

Bilateral trade Switzerland – Hong Kong

	Exports (CHF million)	% Change	Imports (CHF million)	% Change	Trade Balance	Total Imp./Exp.	% Change
1990	2'265	4.3%	902	-17.3%	1'363	3'166.8	-
1995	2'843	-10.0%	642	-4.3%	2'201	3'485.3	10%
2000	3'842	31.9%	895	36.3%	2'947	4'736.1	32.7%
2001	4'039	5.1%	679	-24.1%	3'360	4'718.6	-0.4%
2002	4'479	10.9%	824	21.3%	3'655	5'304	12.4%
2003	4'002	-10.7%	648	-21.3%	3'353	4'650.9	-12.3%
2004	4'073	1.8%	822	26.6%	3'251	4'894.2	5.2%
2005	4'012	-5.3 %	1'674	52.4%	2'338	5'686	16.2%
2006	4'694	17.0%	1'457	-13.0%	3'237	6'151	8.2%
2007	5'296	12.8%	1'185	-18.6%	4'111	6'481	5.4%
2008	6'203	17.1%	1'440	21.5%	4'763	7'643	17.9%
Jan-June 2009	**2'726**	**-1.5%**	**498**	**-34%**	**2'228**	**3'224**	**-8.5%**

Major products

Exports	2007		2008		
	% of total	CHF million	% of total	CHF million	% Change 2007/2008
1. Watches and clocks	46	2'432	44	2'697	11
2. Jewellery and precious stones	29	1'523	35	2'143	41
3. Chemical and pharmaceutical products	8.3	438	7.3	454	3.6
4. Machinery	8.3	440	6.2	382	-13

Imports	2007		2008		
	% of total	CHF million	% of total	CHF million	% Change 2007/2008
1. Jewellery and precious stones	53	626	59	853	36
2. Watches and clocks	22	257	20	292	13
3. Machinery	12	143	9.8	141	-1.4
4. Textiles and garments	4.7	56	3.2	46	-19

Appendix 5

Major investor countries/regions 2007

Rank	Country/Region	Direct investments (USD billion)	Share (%)	Growth (%)	Change of inflow (USD billion)
1	China	479	41%	84%	-0.6
2	British Virgin Islands	431	37%	72%	3.9
3	Netherlands	68	5.8%	36%	1.3
4	Bermuda	49	4.2%	8.9%	0.5
5	USA	36	3%	0%	-2
6	Japan	21	1.8%	11%	-0.5
7	UK	17	1.4%	21%	1
8	Cayman Islands	14	1.2%	7.7%	-1
9	Singapore	14	1.2%	27%	1.1
10	Taiwan	5.1	0.4%	19%	-0.8
	EU	96	8.1%	34%	5.4
13	**Switzerland**	**4.1**	**0.4%**	**0%**	**0.03**
	Total	1,178	100 %	59%	9.5
Rank	**Country/Region**	**Portfolio investments (USD billion)**	**Share (%)**	**Growth (%)**	**Change of inflow (USD billion)**
1	China	166	21%	68%	N.A.
2	Cayman Islands	132	17%	71%	N.A.
3	Bermuda	104	13%	63%	N.A.
4	UK	74	9.5%	2.8%	N.A.
5	USA	71	9%	9.2%	N.A.
6	Australia	43	5.5%	0%	N.A.
7	Luxembourg	27	3.5%	29%	N.A.
8	Japan	21	2.7%	11%	N.A.
9	Republic of Korea	20	2.6%	43%	N.A.
10	Ireland	17	2.2%	89%	N.A.
22	**Switzerland**	**2.4**	**0.3%**	**85%**	N.A.
	Total	782	100%	35%	N.A.

*N.A. Not available

Sources : Hong Kong Census & Statistics Department, IMF