

HONG KONG

Economic Outlook for the 1980s

By Toyomitsu Tamao

Factors behind high growth in late 1970s

Among the Asian NICs (newly industrializing countries; South Korea, Taiwan, Hong Kong, and Singapore), Hong Kong recorded the greatest economic growth in the 1970s. The Crown Colony's average annual growth rate of 13% in the second half of the decade was little short of astonishing.

In forecasting Hong Kong's economy in the 1980s, it may be useful to start by examining the background to the colony's super-high growth during those five years. Rapid export growth in 1976 triggered the recovery of the world economy from the 1974-75 recession. Hong Kong's economic recovery, too, was spurred by a real 30% increase in exports of locally manufactured products. Exports of local products account for a high percentage (around 60%) of Hong Kong's gross domestic product. The recovery in exports of local products stimulated the colony's total economy through two complementary processes; rapid revival of employment → wage increases → expansion of consumer demand; and rapid rise in factory operating rates → increase in corporate profits → recovery of plant and equipment investments.

More noteworthy than this, however, was the far-reaching impact that China's return to the international economic scene had on Hong Kong's economy. China proclaimed its "Four Modernizations Policy" in 1978 and adopted a positive approach to economic exchange with countries in the Western camp. This bolstered confidence in Hong Kong's future.

Britain and China differ in their interpretations of whether or not the New Ter-

ritories, comprising 92% of the total area of Hong Kong, fall under the area leased by treaty to Britain until 1997. Thus, every time a political upheaval occurred in China in the past, apprehensions rose over the future of Hong Kong, affecting both the real estate and stock markets.

China's 1978 shift to her "Four Modernizations Policy" was interpreted in Hong Kong and abroad as guaranteeing the long-term stability of the territory and economic system of the Crown Colony. The shift also led the world to reassess the future potential of the latent Chinese market.

This historic development overturned the conventional wisdom that the Hong Kong market is limited to its narrow jurisdictional land area. The credibility of Hong Kong's future status rose to unprecedented heights, triggering a real estate boom and greatly stimulating construction activities. This, together with brisk exports, resulted in aggressive plant and equipment investment.

As the world reassessed the role of Hong Kong as a base for doing business with China, now and in the future, foreign corporations, and investment, flooded into the colony. Many Chinese government agencies also opened offices in Hong Kong to expedite the modernization process. China also rapidly increased her investments in the colony, including the expansion of existing bases.

The Hong Kong government itself vigorously pushed development of the infrastructure, including government housing, a subway system and industrial complexes.

These activities resulted in a substantial increase in gross fixed capital formation in the colony (average annual real growth rate 19%), laying the foundation for tremendous economic growth.

The increase in worker income in the manufacturing sector, coming as a result of buoyant exports, and the rise in living standards brought on by the growth of the total economy, caused personal consumption to expand at an average annual growth rate of 13%. Nor should it be overlooked that the factor which sustained the growth of personal consumption was a change in Hong Kong's population structure.

A look at the pyramid chart of Hong Kong's population shows that at present the largest population segment is the 20-25 year age group, followed by the 15-19 segment. This means that in the latter 1970s a large number of young people not only entered the labor market to earn income but also joined the consumer market. This induced a consumer revolution, as evidenced by the mushrooming of boutiques, electronic game centers, discotheques, and fast food restaurants.

It is believed that Hong Kong's per capita GDP passed the US\$3,000 level in 1976-77. The experience of other advanced countries shows that a mass consumption boom follows when this level is passed. It can be assumed that the increase in assets resulting from the real estate and stock boom, mirroring the new confidence in Hong Kong's future, gave further impetus to personal consumption.

Certainly the recovery in exports was the trigger which launched the super-high growth Hong Kong's economy experienced in the latter half of the 1970s. However, this was still economic growth led by domestic demand because of structural changes brought about by China's approach towards the West and the change in the population structure. Hong Kong had in effect divested itself of its tradi-

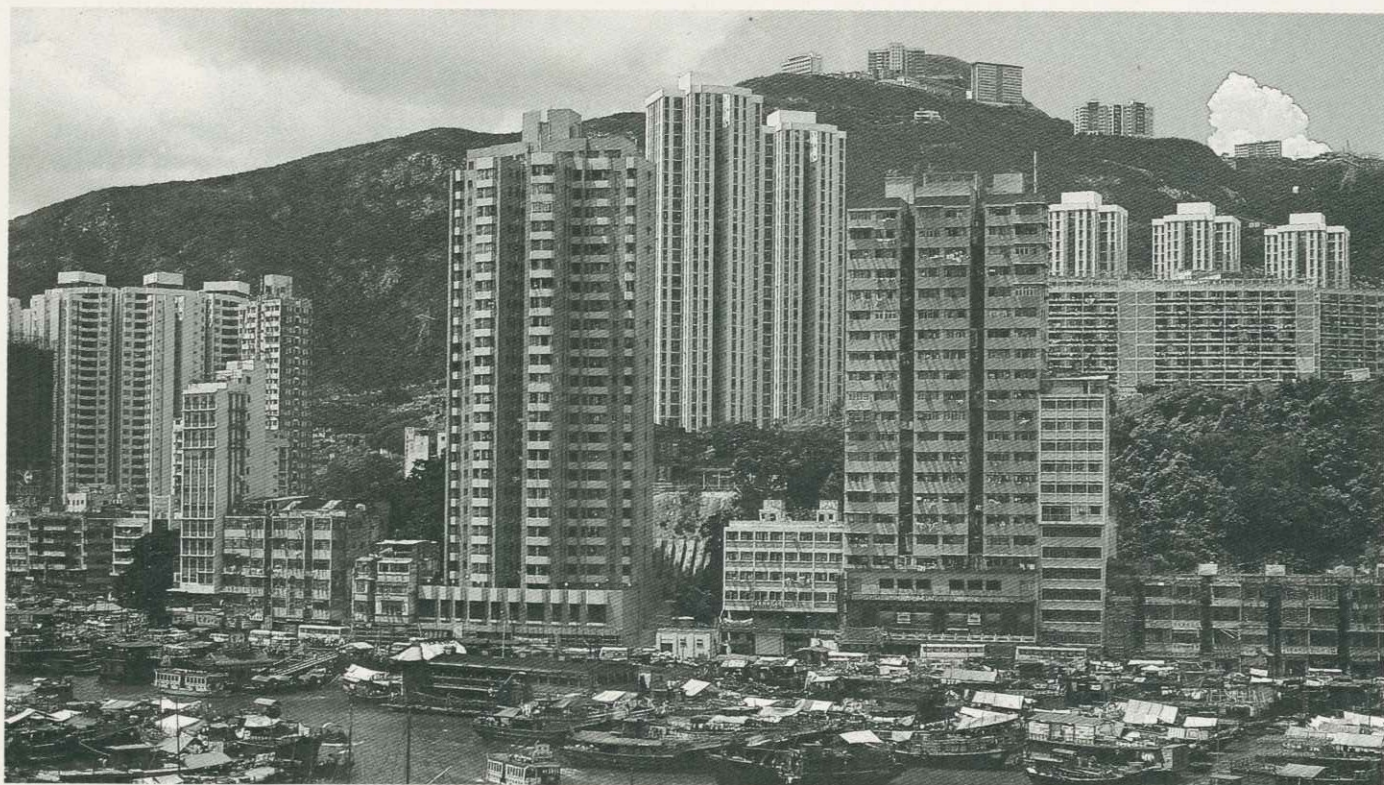


Photo: PPS

tional image of an economy moving in parallel with exports. But it also meant that the Crown Colony could, and has, experienced such distortions as a sharp increase in its trade deficit because of imports mounting faster than exports, inflation, high interest rates, and the depreciation of the Hong Kong dollar vis-à-vis other currencies.

Renewed uncertainty and economic confusion

Although clouds began to appear on the export horizon in mid-1980, the overheated, domestic demand-led economic boom continued through 1981. But by the beginning of 1982, the export slump, reflecting the global recession, had become more clearly defined. At the same time, uncertainty over the future of Hong Kong suddenly resurfaced.

This came in the form of an announcement prior to June 30, 1982, exactly 15 years before the expiration of Hong Kong's lease on June 30, 1997, that Prime Minister Margaret Thatcher would visit Beijing. Financial circles, which would be unable from July to conclude 15-year loan contracts, began to demand an early solution to the "1997 problem."

During Thatcher's visit to China in September, the leaders of Britain and China confirmed the determination of both countries to sustain Hong Kong's prosperity and negotiate a concrete solution to the lease problem through normal diplo-

matic channels. However, it soon became clear that the two sides were at odds over the basic interpretation of the question of sovereignty, and hopes for an early settlement faded. Pessimism over Hong Kong's future ballooned, and the Hong Kong dollar, stocks and real estate prices tumbled.

The collapse of the overinflated real estate bubble and its widespread impact came on top of the slump in the manufacturing sector as exports slowed. As a result, the economic growth rate slipped with each new quarter in 1982, dropping to an estimated 4% in the fourth. The real growth rate in 1982 plummeted to 2% from 11% in 1981.

Prospects for the mid- and late 1980s

In order to forecast the future of Hong Kong, it will be necessary, as indicated by the above historical review, to approach the subject from three angles: first, export trends; second, relations with China; and third, structural change within Hong Kong itself.

Hong Kong's economic system is based on private enterprise, and adheres almost completely to the principle of free competition. In its economic relations with the outside, Hong Kong has no national borders and maintains close-to-perfect free trade and free foreign exchange systems. It also ascribes to the principle of non-discriminatory treatment for all capital investment, whether by domestic or by

foreign enterprises. The Hong Kong government keeps intervention in business affairs to a minimum.

This means that Hong Kong's economy mirrors international economic trends very closely. It also means that its economic structure is quite flexible. Because the automatic mechanisms to adjust wages, land prices and commodity prices operate more efficiently in Hong Kong than in competing countries, the Crown Colony does not lose its international competitiveness easily. This year, its exports, mainly those to the United States and China, have been recovering more strongly than anticipated.

In terms of Hong Kong's political relations with China, it goes without saying that the most important point will be the form of the settlement that is reached on the "1997 problem."

This is a high-level political problem, and negotiations on the diplomatic level are already underway between Britain and China. One should refrain from making rash predictions, but the probability is high that the transfer of territorial sovereignty to China will take place, and that Hong Kong's present economic system will be maintained. This is because Hong Kong's present prosperity is not dependent on such "hardware" aspects as its geographical location and highly developed infrastructure. Rather, it depends very much on the "software" side, exemplified by principles of economic management and the economic system.

Moreover, Hong Kong's prosperity is

indispensable for the acceleration of China's modernization. This is because by keeping Hong Kong prosperous, China will be able to maintain the trust not only of the people of Hong Kong but also of foreign businessmen. The maintenance of such trust, furthermore, can serve as a realistic preparation for the eventual integration of Taiwan into China.

Hong Kong's economic relations with China include oil development in the South China Sea, tieups in the manufacturing sector with China, Chinese investment in Hong Kong, and expanded trade with its giant neighbor.

Regarding South China Sea oil development, a consortium led by British Petroleum Development obtained the first concession in May 1983. Other consortiums are expected to obtain concessions as the months go by, and actual drilling should get into high gear in the near future, with production expected to start around 1986. It is expected that the South China Sea oil wells will be producing 80 million tons of crude oil annually in 1990. This would amount to 80% of all of China's offshore oil production.

As the main production area will be off Zhujiang, it is quite possible that petroleum-related industries will be established on the Zhujiang coast. It is expected that Hong Kong would play a very big role in providing software support, including financing and services, for such industries.

The possibility of the Crown Colony's manufacturing sector linking up with China also deserves special attention, as this would give Hong Kong an advantage other Asian NICs do not possess. A survey conducted recently by the Hong Kong Clothing Manufacturers Association of its 450 member companies revealed

that 9.3% of them were already using China as a processing base and have succeeded in reducing production costs. A tieup with China will enable Hong Kong manufacturers to devote their efforts to product and market development, thus orienting Hong Kong's industrial structure toward higher value added and advanced technologies.

Hong Kong's exports of local products to China in 1982 totaled HK\$3.8 billion, an increase of 122 times over the 1977 figure. Re-exports totaled HK\$8 billion, an increase of 46 times over 1977. The total re-export of Chinese products via Hong Kong was valued at HK\$14.7 billion, six times what it was in 1977. Although these growth rates will inevitably slacken, Hong Kong's trade volume with China can be expected to continue to expand in parallel with the progress of China's modernization.

Finally, let us examine the factors which will influence structural change within Hong Kong. The younger generation, which at present constitutes the largest age strata in Hong Kong's population, will age. The rate of growth in the supply of new young labor has been declining since the latter half of the 1970s. In absolute terms, however, young labor is expected to continue to increase through the first half of the 1980s, then see a gradual decline in the second half of the decade.

In contrast, the married population will increase steeply, and the accompanying increase in housing demand and the invigoration of the consumer market can be expected to continue through the 1980s.

Another point that should be noted is a generational change among overseas Chinese industrialists, a process which actually began in the late 1970s. The majority of

Hong Kong industrialists moved into the Crown Colony immediately before or after the establishment of the People's Republic of China in 1949. Most are now in their sixties or seventies and are expected to hand over control to the next generation during the 1980s. The majority of the second generation have been educated in universities in Hong Kong or in the United States and Europe and are familiar with modern management techniques, and possess a cosmopolitan outlook. Being full of youthful vitality, they can be expected to boldly expand their businesses and venture into new fields. Their vitality will rub off on Hong Kong's entire economy.

Conclusion

If one is not overly pessimistic about the world economy in the 1980s and the settlement of the "1997 problem" (and given the present international environment and on the basis of logically drawn conclusions, I personally am very optimistic on both these counts), one would find in Hong Kong's economic situation many factors which will have vitalizing effects, and which should lead to new business opportunities. Therefore, I believe that Hong Kong will be able to sustain a high growth rate in the 1980s.

Hong Kong will likely retain its economic attraction as the geographical center of the East and Southeast Asian regions—considered the high-growth areas for the world in the 1980s and 1990s—and the southern gateway to China, predicted to be the economic power of the 21st century. Foreign corporate participation and investments in Hong Kong will continue.

Hong Kong's real economic growth was 9% in the second half of the 1960s; 7% in the first half of the 1970s; and 13% in the second half of the 70s. My personal projection is that the 1980s will see 7–8% growth in the first half, and 10–12% in the second.



A busy Hong Kong street indicates the level of expansion of personal consumption.

Photo: PPS/P. J. Griffiths/Magnum

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