

Why the European Union should care about Hong Kong.

By Willem van der Geest*

The Hong Kong Society's Chinese New Year's dinner in Brussels was a grand and marvellous occasion, with the Hong Kong Academy of Performing Arts demonstrating its exceptional musical talent as its young musicians and dancers displayed intensity and beauty. The Hong Kong Secretary for Trade delivered a truly seductive message on this eve of the year of the pig – come to Hong Kong and get rich! But was Brussels – official home of the heart and the mind of the European Union – attentively listening or merely watching detachedly as it enjoyed the Society's hospitality?

Most European analysts argue that the 1997 transfer of sovereignty from Britain to China means that Hong Kong matters are now to be left to its citizens and the Beijing central government. Most also would agree that the EU can have a positive impact on developments in Hong Kong and can contribute to its remaining on a feasible path towards multi-party democracy on a sensible time-table, as well as seeking improved economic access for EU business. However, only few feel that it has any moral responsibility to engage in and monitor the implementation of the Basic Law, agreed between China and the UK, either in the economic or the political domains.

European Perceptions of EU-Hong Kong relations

European analysts believe, off-the-record, that the central government in Beijing would perceive such interest in Hong Kong as meddling in its internal affairs. Nobody wants another unwelcome irritant, perhaps even a stumbling block, in the ever closer and all-important EU-China relationship. While endorsing the importance of constructive EU-China relations, the EU even so should use its soft power politics judiciously but strategically, while standing firm on its core principles of democratization, rule of law and an economically level playing field for Chinese and EU companies in Hong Kong, still an important gateway to the mainland.

The European Union's interest in Hong Kong remained intense in the immediate post-97 years– not least because of the 1999 appointment of its former Governor, Chris Patten, as the European Commission's Commissioner for External Relations. His close contacts in Hong Kong political and business circles rivalled that of his staff – and he remained intensely interested. Ever since the EU opened its Hong Kong office in 1993, it has sent highly gifted delegates there, including a French PhD in law and political science who came originally from Shanghai as well as the EU's former Asia Europe Meeting (ASEM) counsellor. But was there anything much for them to do in their well-located offices in Garden Road?

The European Union, inevitably, has a complex working method because policies and instruments are the result of compromise and coalition leading to common positions. In Brussels it is sometimes said, only half-jokingly, that ‘...some common positions are more commonly held than other common positions.’ How widely would an ‘active’ Hong Kong policy by the EU be supported by its member states? What might be its substance and what could be the instruments for implementing such a policy?

Opportunities for EU-Hong Kong Cooperation

The EU Commission’s official Communication to the Council and the Parliament on Hong Kong and Macao outlines ‘possibilities for cooperation 2007-2013’.ⁱ This time frame coincides with the EU’s long term budget, known in Brussels jargon as ‘financial perspectives’, adopted for the seven-year period after lengthy debate. Significantly, the budget lines for the EU’s international cooperation with industrial countries permit a financial allocation for Hong Kong, providing for the first time the resources needed for a genuinely ‘active’ policy.

The case for greater engagement starts with the long-standing EU interests in Hong Kong. There is a great deal of two-way trade; if transit trade via Hong Kong to China is included, Hong Kong ranks as the sixth most important bilateral trading partner. As a gateway to China, its trade with the EU remains close to €30 billion (US\$40 billion). The EU is Hong Kong’s third largest supplier, after China and Japan, and the third largest investor. About one of four banks licensed in Hong Kong were incorporated in the EU, as were one of six insurance companies, making the EU the top overseas insurer. The Hong Kong 2007 growth outlook is a strong 5%, according to the Asian Development Bank, and Hong Kong’s transparency ranking is high, well above that for most EU member states and far ahead of the mainland.ⁱⁱ Its investment climate remains highly attractive to EU companies.

But of course policy is not only about trade in goods and services: over 45,000 EU citizens reside in Hong Kong. Its civil service, even today, relies on critical inputs from UK and other EU citizens. One of four foreign companies based in Hong Kong originates from the EU. It is a key destination for European tourists, while educational exchanges remain prominent. The days when a young lawyer needed to go to London, Oxford or Cambridge to be called to the Bar-at-Law or sit a Masters in Law exam are over, but the interest of young Hong Kong citizens in gaining internationally accredited degrees and professional qualifications is as strong as ever. For example, the association certifying chartered accountants (ACCA) finds that its fastest growing number of members come from Hong Kong and China, encouraged by its president, Sam Wong. Although Singapore was the destination of choice for the French business school INSEAD, it is safe to assume that Hong Kong before long will attract a major off-shore centre of a leading global university or business school.

The EU Communication identifies comprehensive possibilities for additional cooperation, and lists seven major areas: trade and customs; finance; people-to-people links (including academic); transport; the environment; health and food safety. In the

trade and customs domain, the specific areas include consultation on bilateral and multi-lateral issues, such as the World Trade Organization talks, customs cooperation to combat counterfeiting as well as to improve maritime safety, and also support for business, especially small and medium enterprises. For the financial services sectors, the focus would be on regulatory dialogue as well as improved governance in tax matters to avoid evasion. People-to-people contacts including academic exchanges offer many untapped opportunities, to be stimulated through Erasmus and Jean Monnet fellowship programs, as well as through enabling joint bidding for EU research framework programs. Immigration cooperation should continue, while the EU's visibility could be enhanced through a 'Europe House'. Transport cooperation in the maritime safety and aviation fields could be reinforced through new agreements, in view of the vital role of Hong Kong's harbour and airport vis-à-vis China as well as for the wider Asia-Pacific region. Public health and food safety cooperation, after SARS and in the face of avian influenza, has taken on renewed importance. Finally, environmental cooperation would seek to reinforce and deliver action on climate change as well as the fight against air and water pollution.

Coordination with EU Member States

The UK position on Hong Kong is now finely synchronized with that of the European Commission, as stated by Geoffrey Hoon, Minister for Europe, in the House of Commons. He said the EU Communication is "consistent" with the UK Government's own assessment that the "one country, two systems" principle generally has worked well in practice. He also said that there is "...still a need to make progress towards universal suffrage" and that Hong Kong should adopt such a system "as soon as possible". He endorsed the Commission's view that China's "exponential" economic growth has created new opportunities for Hong Kong, and agreed there is great potential for further development of relations between the EU and Hong Kong, with a focus on key areas of common competence listed above. This ringing endorsement from the UK, inevitably the major EU player as regards Hong Kong, has given the Commission an extra degree of freedom for developing an 'active' Hong Kong policy.

Building blocks or Stumbling blocks for closer cooperation?

But the Commission also raises the sensitive question of competition policy, noting that European companies often complain about the lack of a level playing field in certain key sectors. The withdrawal of the French retailing giant Carrefour in September, 2000 is still vividly remembered. It closed its Hong Kong stores, claiming an 'inability to access large enough sites for its hypermarket style of operation'.ⁱⁱⁱ Yet the retailing giant has strengthened its presence in mainland China, where it first opened in 1995, and is now the leading foreign retailer—with 92 stores at the end of 2006, mainly in Beijing and Shanghai, and 20 more planned for 2007. The Hong Kong Democratic Foundation has been campaigning for anti-monopoly and anti-trust legislation, calling the present competition framework ineffective. Severe cases of market-rigging are seldom pursued and the interlocking of land ownership, property development and share-holding of

commercial enterprises continues to be a formidable non-tariff barrier to the EU's trade and commercial presence.

This has been noticed in Brussels. Pascal Lamy, the previous EU Trade Commissioner who is now Director-General of the WTO, exchanged letters about competition policy with the Hong Kong Democratic Foundation. He called the absence of a competition law costly for consumers at large and competitors in particular. He noted that phasing out government monopolies without sound competition laws will mean that private trade barriers can all too easily be erected or reinforced. He also quite pointedly referred to the need for a ban 'on hard core cartels such as the Vitamins Cartel, which is believed to have resulted in massive overcharges for consumers, including in Hong Kong'.^{iv}

From within Hong Kong, interest groups, such as the Consumer Council, have provided evidence of collusive practices and anti-competitive behaviour. Policy think tanks, like Christine Loh's Civic Exchange and the Democratic Foundation, have proposed feasible and workable structures to address the issue. But follow-up has been feeble.

The Commission also raises the question of intellectual property rights violations, noting that Hong Kong remains the source of 8% of all recorded violations in the EU. In addition, the US Department of State's most recent annual report on economic and commercial relations with Hong Kong, required by the Hong Kong Policy Act of 1992, provided some industry estimates of IPR and copy-right infringements. For example, it reported a software industry estimate that Hong Kong's software piracy rate was 52% in 2004, higher than in other advanced economies, resulting in losses of \$116 million to rights-owners.

However, this is still a great deal better than the reality in mainland China, if one is willing to accept industry estimates. For 2004, the incidence of software piracy is believed to be 90%, with motion picture copyright infringement running at 95%. Earnings lost on entertainment software in the mainland are estimated at \$510 million. Even more visible is book publishing, with two of every three copies of Harry Potter sold in China believed to be pirated, a record very closely followed by Bill Clinton's *My Life*.^v The US customs agency has reported that two-thirds of the counterfeit goods it seizes originate from China.

Arguments for an 'active' Hong Kong policy

The arguments for an 'active' Hong Kong policy, rather than one of benign neglect, are ultimately based on its unique role vis-à-vis mainland China. The recent Shanghai stock market volatility has reminded investors about the fragility of China's regulatory framework and questions about the vulnerability of its economic boom remain. No stock exchange is safe from investors' jittery reactions, but the Hong Kong exchange is better equipped to address volatility and challenge than is the Shanghai exchange. And even the evidence of counterfeiting and IPR infringements, worrying though it may be, could lead one to favor an active policy. Enforcement of the IPR regime in Hong Kong is definitely

better than that in mainland China. In effect, Hong Kong can provide a model for dealing with counterfeiting and IPR infringement inside China.

Precisely because Hong Kong remains an important gateway to China, though by no means the only one, what happens in its territory has implications for the mainland. In a sense, Hong Kong is a testing ground and laboratory for eventual reforms in the mainland.

This argument is not merely limited to the functional fields of cooperation identified by the Commission. The ultimate experiment which may be conducted in Hong Kong, and will be closely watched by the mainland, is one of a gradual movement toward universal suffrage for the election of its Chief Executive. Such a controlled experiment, ostensibly in 2012, will critically affect the shape of possible reform in the mainland. And that is when a more active EU involvement in Hong Kong's political and economic development will find its pay-off.

About the Author:

Willem van der Geest is an economist who specializes in economic development and international political economy. He has a PhD from Cambridge University and is CEO of the Brussels-based Asia Institute Europe, a recently founded think tank working on research and analysis of EU-Asia relations.

ⁱ European Commission, (2006), 'Communication from the Commission to the Council and the European Parliament, The European Union, Hong Kong and Macao: Possibilities for Cooperation 2007-2013, Brussels, 26.10.2006. The Communication, as well as Annual Reports on developments in Hong Kong, are available from the EU's Hong Kong delegation website www.delhkg.ec.europa.eu.

ⁱⁱ Transparency International publishes the corruption perception index and in 2006 ranked Hong Kong at 14, out of a sample of 163 countries, with mainland China ranked 57. Within Asia only Singapore, ranked 4, outperformed Hong Kong. The index is based on surveys of perceptions of corruption incidence prepared by the Economist, the World Bank, Freedom House, the World Economic Forum, IMD and 3 consultancy organisations specialised in comparative political and market risk analysis.

ⁱⁱⁱ Hong Kong Democratic Foundation (2003), *Competition Policy for Hong Kong*, a joint position paper by the Frontier and the Hong Kong Democratic Foundation

^{iv} Letter from Pascal Lamy to Alan Ka-lun Lung, Chairman Hong Kong Democratic Foundation, May 11, 2004 (D/1570)

^v According to Prof Eric Smith offering evidence at a Panel on IPR enforcement, organized by the US Congressional Executive Commission on China.