

The Closer Economic Partnership Arrangement (CEPA): A Win-Win Strategy for Both Mainland and Hong Kong

Lawrence J. Lau, Ph. D., D. Soc. Sc. (hon.)

Kwoh-Ting Li Professor of Economic Development

Department of Economics

Stanford University

Stanford, CA 94305-6072, U.S.A.

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Phone: 1-650-723-3708; Fax: 1-650-723-7145

Email: LJLAU@STANFORD.EDU; WebPages: WWW.STANFORD.EDU/~LJLAU

The Closer Economic Partnership Arrangement

- ◆ An opportunity for both Mainland and Hong Kong
- ◆ A living document rather than a blue-print
- ◆ Expandable broad-based definition--“Economic” can also encompass the environmental, public health, commercial crimes prevention, public safety and the technological
- ◆ The spirit of mutual cooperation for mutual benefit
- ◆ Trade in goods (reduction and elimination of tariff and non-tariff barriers)
- ◆ Trade in services (elimination of discriminatory barriers and treatments)
- ◆ Investment (direct and potentially portfolio investment flows in both directions)

Closer Economic Partnership Arrangement— Trade in Goods

- ◆ Affirmation of zero tariffs for Mainland imports to Hong Kong
- ◆ Tariffs on 273 Hong Kong-made goods, accounting for 67 percent of Hong Kong exports to China, will be completely exempted as of January 1, 2004 (compared to an average tariff rate of 9% by 2007 under the WTO agreement).
- ◆ In addition, tariffs on all other Hong Kong-made goods will be completely exempted by January 1, 2006.
- ◆ However, total tariff savings would amount to just below US\$100 million.

Closer Economic Partnership Arrangement— Trade in Services

- ◆ Firms in 18 (17 originally) service sectors in Hong Kong, including retailers, wholesalers, distributors, logistics companies and shipping lines, will be allowed to set up wholly owned subsidiaries in China sooner and with fewer restrictions than is required under the WTO accession agreement. (However, such firms must have been in operation in Hong Kong for more than three to five years in order to qualify for the preferential treatment.)
- ◆ Banks based in Hong Kong, including Hong Kong subsidiaries of foreign banks, will face a lower threshold in terms of total assets (US\$6 billion compared to US\$20 billion) for entry into the Chinese market.
- ◆ Chinese language movies produced by Hong Kong production companies will not be subject to the Chinese import quota on foreign movies.
- ◆ Renminbi accounts will be permitted for Hong Kong residents and firms.
- ◆ Promotion of tourism in both directions
 - ◆ Chinese citizens from selected cities, (originally Dongguan, Jiangmen and Zhongshan, in Guangdong), China are now permitted to visit Hong Kong for the purpose of sight-seeing as individual tourists. The rate of growth of the total number of Chinese tourists visiting abroad is projected to be more than 20% per annum over the next five years.

The Underlying Principles

- ◆ Adherence to “One-Country, Two Systems”
- ◆ Compatibility with World Trade Organization commitments
- ◆ Identification of areas of common interests and benefits
- ◆ Stable and sustainable long-term partnership
- ◆ Reciprocity of rights and obligations
- ◆ Mutual benefit and equitable sharing (a “Positive-Sum” game)

The Outstanding Practical Issues

- ◆ How to define “Rules of Origin”?
 - ◆ Goods, services, and investments
 - ◆ Substantive business operations
- ◆ Identification of areas of common interest and potential mutual benefit
- ◆ Identification of the core competence/comparative advantage of the Mainland and Hong Kong so as to enable specialization and division of labor
- ◆ “Guest workers” in both directions?

The Implementation

- ◆ Large gains can be realized from the reduction of transactions costs
- ◆ Expediting new start-up businesses under CEPA
 - ◆ One Stop Service at the Central Government, Provincial Government, and City and County Levels on the Mainland
 - ◆ One-stop Service in Hong Kong
- ◆ Information sharing and transparency
 - ◆ The importance of accurate and timely information—multiple independent channels (the case of SARS)

Cooperation of Hong Kong with Its Neighbors

- ◆ Hong Kong as the hub of the Pearl River Delta.
- ◆ Shenzhen-Hong Kong Western Corridor Bridge (the 4th vehicular boundary crossing bridge).
- ◆ Gangzhu'ao Bridge, linking Hong Kong, Zhuhai and Macau.
- ◆ Closer economic and technical cooperation between the Hong Kong and Shenzhen Airport authorities (and perhaps with the others as well)

The Dynamic Comparative Advantages and Core Competences of Hong Kong

- ◆ A stable and convertible currency
- ◆ Free flow of short-term and long-term capital
- ◆ Clear, credible, simple and reliable legal system that governs economic and financial activities
- ◆ Timely and unhindered availability of information
- ◆ Raising education and skill levels of the Hong Kong labor force is the key to Hong Kong's future

Potential Cooperation in Financial Services

- ◆ Listing of Chinese enterprises on the Hong Kong Stock Exchange
- ◆ Encouragement of investment in Hong Kong by Chinese enterprises
- ◆ Dual listing of shares on the Hong Kong and Shenzhen Stock Exchanges

Provision of Services to Mainland Residents and Vice Versa

- ◆ Education (that is why reciprocal recognition and eligibility for examinations is important) at the tertiary level—Hong Kong as an education and training center
- ◆ Health care
- ◆ Private banking and asset management services

Next Steps: Harmonization of Standards on Goods and Services

- ◆ Harmonization of standards (high-definition TV, digitization of audio-video signals, voltages, driving on the “right” side?)
- ◆ Certification of professional practices
 - ◆ Reciprocal procedures and common standards for recognition of degrees and certificates and for qualification
 - ◆ Reciprocal eligibility for participating in qualifying examinations

Next Steps: Harmonization and Rationalization of Taxes

- ◆ Income taxation
 - ◆ Elimination of double taxation of income (by Mainland and Hong Kong) at both the corporate and the individual levels, if any
 - ◆ Simplification of the procedure for the taxation of earnings of non-residents by both Mainland and Hong Kong
 - ◆ Taxation of dividends and interest (mutual exemption?)
 - ◆ Taxation on license fees and royalties
- ◆ Harmonization of external tariffs, if any (e.g., alcohol and tobacco, automobiles)
- ◆ Rebate or exemption of value-added taxes, consumption taxes and sales taxes for exported goods

Cooperation on the Environment, Public Health, Commercial Crimes, Public Safety and Technology

- ◆ Internalization of externalities
 - ◆ Cooperation in the control of pollution
- ◆ Cooperation on public health
- ◆ Cooperation on the investigation and prosecution of commercial crimes
- ◆ Agreement on mutual enforcement of valid judicial judgments issued by each other's courts in commercial disputes (perhaps with a centralized appeal process)
- ◆ Cooperation on crime control
- ◆ Protection of intellectual property rights
 - ◆ Reciprocal recognition/registration of patents, trade marks and other intellectual property rights

Concluding Remarks

- ◆ The success example of the North American Free Trade Area (NAFTA)
- ◆ Both Mainland and Hong Kong can win with CEPA