A Study of Trends and Challenges Facing Hong Kong
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I. ABOUT THE HONG KONG MANAGEMENT ASSOCIATION

Established in 1960, The Hong Kong Management Association (the Association) is an apolitical and non-profit-making organization with the vision to be the leading professional organization advancing management excellence in Hong Kong and the Region.

Vision

To be the leading professional organization advancing management excellence in Hong Kong and the Region

Mission

- To promote best practices in management
- To nurture human capital through management education and training at all levels
- To provide members with a platform for exchange of ideas, networking and personal development

Value

- Continuous improvement
We embrace best practices through continuous improvement.

- Innovation
We welcome new ideas, seek out new skills and capabilities, and explore new concepts.

- Integrity
We are open, honest and forthright in our dealings.

- Professionalism
We strive for excellence in all we do.

- Respect for Individuals
We built relationships based on trust and respect.

- Sustainability
We integrate sustainability into all aspects of our operations and business practices.

Services provided by the HKMA can be categorized into three major areas, namely education and training; management services and membership services.

With a commitment to nurturing human capital through management education and training at all levels, the HKMA offers over 2,000 training and education programmes covering a wide range of management disciplines for more than 50,000 executives every year. From distance learning courses, seminars and workshops, certificates, diplomas, all the way to bachelor, master and doctorate degree programmes in conjunction with prestigious overseas universities, these programmes are suitable for executives at different stages of development. The HKMA also provides specially designed in-house training which geared to the particular needs of different organizations. In 2009, the Association introduced the concept of Corporate University, which helps companies retain quality staff and build a corporate culture of lifelong learning.

The Association believes learning while networking works best for achieving continuous development. Diversified management services are offered to provide platforms for business executives to exchange ideas, to network and to gain professional development. Annually, the Association organizes diverse functions such as Annual Conference, Theme Year Seminars and
Activities and Dinners. Prominent business leaders are invited to share their invaluable insights and wisdom on the most updated trends and development of management.

Business award is another major area of HKMA’s management services. To promote best practices in management, each year, the Association organizes eight business awards in Hong Kong and the Mainland. These include the Best Annual Reports Awards, the HKMA Quality Award, the Award for Excellence in Training and Development, the HKMA/TVB Awards for Marketing Excellence, the Hong Kong Management Game, the Distinguished Salesperson Award, the Award for China marketing Excellence and the China Best Annual Reports Awards for Listed Companies. These prestigious awards, which are now regarded as the highest accolades of the business community, provide an exemplary model for business professionals to follow and benchmark.

With a total of over 13,000 members including individuals and corporates, membership service has always been a priority for the Association. A comprehensive range of membership activities such as seminars, forums, luncheons, company visits, study tours and social gatherings are offered every year. Another distinctive feature of membership is the eight autonomous specialist clubs which provide opportunities for members with similar interests to meet and develop further their specialist knowledge. The highlight event of membership is the Annual Fellowship Dinner which provides an excellent platform for members to extend their network.

II. TRENDS AND KEY CHALLENGES FACING HONG KONG IN 2014/15

Every year, the Association takes a critical look at the economic, social and political factors affecting Hong Kong. This study takes into account suggestions from various members of Council and Management Committees, together with research findings. The following is the present trends and challenges facing Hong Kong in the year.

1. ECONOMIC FACTORS

Recovery Strengthens Yet Vulnerability Remains

Global economic activity has broadly strengthened and is expected to improve further in 2014–2015 from 3% in 2013 to 3.6% in 2014.\(^1\) Downside risks continue to dominate the global growth outlook. In advanced economies, major concerns include downside risks from low inflation and the possibility of protracted low growth, especially in the Euro zone. In emerging market economies, vulnerabilities appear mostly localized with a risk in greater general slowdown because of slow or reverse capital inflows.\(^2\)

European Economy

The European recovery remains intact but got off to a disappointing start in the first three months of 2014, when Gross Domestic Product (GDP) rose by just 0.3% across the 28-strong European Union (EU).\(^3\) Forecasts in early May 2014 from the European Commission had already suggested that the recovery would be modest in 2014 but begin to gather momentum in 2015. The GDP in the EU is anticipated to expand by 1.6% in 2014 and 2% in 2015. Anticipated growth in 2014 would not be able to counter low inflation, prompting further monetary stimulus from the European Central Bank.\(^4\) The annual rate of inflation in the 18 countries that use the Euro as its effective currency fell back to its lowest level in more than four years during May 2014. The EU’s statistics agency reported consumer prices rose by just 0.5% in the 12 months leading to May 2014, down from 0.7% in the 12 months leading to April 2014. Low inflation makes it more difficult for Governments, households and businesses to reduce their debts.\(^5\) The European Central Bank, which targets inflation of just below 2%, left interest rates unchanged at 0.25% in March 2014 and has argued that deflation risks in the European bloc are limited. However, there are some signs the euro zone’s economy is on the mend, with the unemployment rate falling to 11.7% in April 2014, the lowest level since October 2012.\(^6\) Retail sales in the euro zone registered their strongest annual growth in seven years in April 2014. Sales in the 18 Euro currency countries jumped by 2.4%, following on from upwardly revised growth of 1% in March 2014. The overall picture remains fragmented. Germany, the bloc’s largest economy, saw retail sales falling on the month of April 2014 for the first time in 2014.\(^7\) An index of household confidence in the Euro zone decreased unexpectedly in June 2014 to negative 7.4 points from negative 7.1 points in May 2014, indicating
the region still faces a difficult economic recovery. The International Monetary Fund encouraged the European Central Bank to engage in a stimulus programme including a large-scale asset purchase to boost confidence, improve corporate and household balance sheets, and stimulate bank lending.

US Economy

The US economy suffered its worst performance for five years in the first quarter of 2014. The economy shrank at an annualized rate of 2.9% in the first three months of the year. This was partially due to the unusually cold weather in the first quarter of the year and the economy benefited from a sharp recovery during the second quarter, posting a growth of 4.5%. The US Federal Reserve cut its growth forecast for 2014 in part due to the harsh winter weather. The Central Bank predicted growth of between 2.1% and 2.3% for the second quarter of 2014, down from its March 2014 forecast of 2.8% to 3%. Consumer spending, which is responsible for more than two-thirds of US economic growth, increased by 1% in the first quarter of 2014, rather than the 3.1% rate as first estimated. The US created 288,000 new jobs in April 2014 and the unemployment rate fell to 6.3%, which was the lowest level since 2008. Under the quantitative easing policy, the Federal Reserve had been buying US$85 billion worth of long-term bonds per month. On 16 April 2014, the Federal Open Market Committee announced a fourth US$10 billion reduction to its quantitative easing program, reducing its monthly bond purchases to US$45 billion in April 2014. Then on 29 October 2014, the Federal Reserve announced that it would cease all bond purchases which indicated that growth in economic activity had picked up. However, the committee reaffirmed its commitment to low interest rates. The target range for the federal funds rate has been 0% to 0.25% since December 2008.

The plan of winding down the economic stimulus programme by the Federal Reserve is expected to push mortgage rates higher. A combination of higher mortgage rates and a surge in prices due to a lack of properties available for sale have weighed on the US housing market since the second half of 2013. However, data from the second quarter of 2014 suggested the housing market was beginning to improve. Sales increased by 18.6% in May 2014 to a seasonally adjusted annual sales rate of 504,000 houses, which was the highest level since May 2008. The US stock market reached a record high as low interest rate gives investors less investment alternatives and easier access to capital. Overall, the projection of the US economy remains positive with the expected unemployment rate to be at 5.8% to 6.1% by the fourth quarter of 2015. GDP growth is projected to accelerate to 2.8% in 2014 and to 3% in 2015.

China Economy

China's economy grew at its slowest pace in 18 months at the start of 2014. China's GDP expanded by 7.4% in the first quarter of 2014. As compared with previous figures, it raised concerns that economy was losing momentum. China's extensive crackdown on corruption in government and business had taken a small, but measurable, toll out of the country's economic growth. It was estimated that the clean-up drive may have shaved GDP growth for the full year by 0.1 to 0.2 percentage points, or about RMB120 billion.

Despite the slowdown of economic growth in the first quarter of 2014 and the impact on anti-corruption campaign, data provided fresh signs that the economy was stabilizing, aided by targeted stimulus measures from Beijing. Retail sales in May 2014 rose 12.5% on a year on year basis and it is the best performance since December 2013. Purchasing Managers’ Index from HSBC rose to a seven-month high of 50.8 points in June 2014, supporting Premier Li Keqiang’s contention that the economy will avoid a hard landing as the government steps up efforts to maintain growth. An index number above 50 indicates expansion.

Premier Li Keqiang asserted in the National People's Congress’s meeting that China had set its GDP growth target for 2014 at 7%, the same as for 2013, and will keep consumer inflation at 3.5%. To sustain the economic growth momentum, the Central Government announced modest measures, such as tax cuts for small firms and speeding up investment in railway infrastructure, to try to steady growth without disrupting plans to restructure the economy or worsening problems of overcapacity, inflation and debt. The impact of shadow banking are evident, as China’s deeply indebted local governments had relied on the sector to raise funds for housing and infrastructure projects. According to The China Banking Regulatory Commission's report, shadow banking...
sector accumulated to RMB 33 trillion in mid-2013, which is equivalent to 80% of China's GDP. Rapid expansion of the shadow banking sector entailed risks of some parts of the business. This prompted the Central Government to issue a series of rules aiming to stagnate shadow banking's growth and minimize the risks to the financial system. The Chinese Central Bank issued a decree in May 2014 mandating that commercial banks should limit its interbank borrowing to less than a third of its liabilities.23

**Hong Kong Economy**

The Hong Kong economy is growing moderately. In the first quarter of 2014, GDP grew by 2.5% in real terms over the first quarter of 2013, but the growth was slightly lower than that of 2.9% in the last quarter of 2013. Due to the temporarily sluggishness of the US economy and the weak demand conditions in the advanced economies weighed on the regional trade flows in Asia. This in turn, worsened the performance of Hong Kong’s exports to major markets. Total exports of goods compiled under the GDP accounting framework slowed to a 0.5% year-on-year growth in real terms in the first quarter of 2014.26 The HSBC Hong Kong Purchasing Managers' Index (PMI) posted above the 50.0 n-change mark at 50.4 in July 2014, signaled a marginal improvement in Hong Kong's private sector operating conditions. Nonetheless, it was the highest headline PMI reading for five months.27

The first-quarter slowdown of GDP growth in Hong Kong was due mainly to weaker private consumption as it accounts for two-thirds of total GDP.28 Although private consumption expenditure grew further by 2% year-on-year in real terms in the first quarter of 2014, it showed a significant slow down as compared with 2013.29 Amidst pressures of falling house and equity prices, the growth in private sector consumption was softened due to adverse wealth effects.30

The residential property market remained stagnant in the first quarter of 2014 amid uncertainty over future US monetary policy and Government's further demand management measures of special stamp duty (SSD) and buyer’s stamp duty (BSD) introduced in late February 2013. Trading volume during the first quarter of 2014 fell further by 34% from the corresponding quarter of 2013 and by 9% from the preceding quarter. Residential property prices edged lower by 1% during the first quarter of 2014. Despite the consolidation in recent months, overall flat prices in March 2014 still exceeded the 1997 peak by 41%, with the housing affordability ratio staying elevated at around 56% in the first quarter of 2014.31

Although the outlook for the Mainland’s economy remains challenging, Hong Kong shall continue to benefit from increasing economic cooperation with China. The Hong Kong Chapter of China's 12th Five-year plan emphasizes the Central Government’s support for the future development of Hong Kong in the following three areas: (1) consolidating and enhancing Hong Kong's position as an international financial, trade and shipping center; (2) support in nurturing emerging industries and developing six new pillar industries; and (3) deepening economic cooperation between the Mainland and Hong Kong through the Mainland-Hong Kong Closer Economic Partnership Arrangement (CEPA).32

On top of the provisions granted in earlier phases of CEPA, the Supplement X to CEPA was signed on 29 August 2013. This provided for a total of 73 services liberalization, trade and investment facilitation measures that aimed to strengthen Hong Kong and the Mainland's cooperation in areas of finance, trade and investment facilitation of the two economies. The new measures came into effect on 1 January 2014.33 CEPA highlights the ongoing commitment of both Hong Kong and the Mainland to eliminate barriers on trade in goods and services. Hong Kong companies as well as professionals should continue to benefit from such measures.

**Strengthening Hong Kong’s Financial Industry**

Hong Kong’s economic prosperity depends much on its continued success in maintaining its status as an international financial centre. Hong Kong plays a unique role as a geographical and metaphorical gateway between China and the rest of the world. Owing to its distinctive history, Hong Kong has a world-class market with international outlook. The Hong Kong Dollar is a free currency with no foreign exchange controls and is pegged to the US dollar.34 The legal system and market regulatory regime are held in high regard internationally.35 The ample pool of skilled
professional talent combined with efficient infrastructure all translates to the development of Hong Kong into a leading international financial centre.

Hong Kong is one of the market leaders in global Initial public offering (IPO) of listed securities. As of 31 December 2013, Hong Kong came second in terms of IPO funds raised, led by the New York Stock Exchange and trailed by the London Stock Exchange, Nasdaq and Tokyo Stock Exchange. Companies raised US$21 billion from IPOs in Hong Kong in 2013, as compared to US$11.5 billion in 2012. Moving onto 2014, the accumulated funds raised in the first quarter of 2014 reached HK$46 billion which represented an impressive 461% year-on-year increment from the first quarter of 2013. The auspicious start gave the market a positive outlook for 2014 and it is anticipated that both IPO proceeds and the number of IPO cases would be higher than 2013.

Nevertheless, Hong Kong’s IPO market is facing steep challenges. The city’s stock market is contending with several obstacles obstructing its IPOs. These obstacles include rising market competition from other exchanges, the need to offer compliance flexibility for potential IPO candidates and the risk of exogenous factors in the local, regional and international perspective.

The Hong Kong Stock Exchange is facing firm rivalry from other exchanges in the region. The Singapore Stock Exchange and the China Securities Regulatory Commission announced a Direct Listing Framework for PRC Incorporated Companies to list in Singapore. Under this framework, qualified Mainland companies meeting listing requirements could undergo minimum corporate restructuring to list on the Singapore Stock Exchange, thereby streamlining the costs and timeframe for Mainland companies seeking IPOs. The framework took effect on 26 November 2013 and will undoubtedly put pressure on the Hong Kong Exchange as potential Mainland IPO companies could explore an additional avenue of going public.

In addition to challenges from other exchanges, the rigidity of the Hong Kong securities regulator posed an immediate and costly threat to the competitiveness of the exchange. The prime example that warranted the most attention in 2014 was the case of Alibaba, the Mainland e-commerce conglomerate which sought to launch the largest IPO in human history. Due to the fact that Hong Kong’s listing rules do not allow the dual-class shareholding structure that has been the foundation of Alibaba’s equity structure and a lack of compromise on both sides, the gigantic Alibaba IPO opportunity went to the New York Stock Exchange. Alibaba’s shares soared 38% in their first day of trading on 19 September 2014 at the New York Stock Exchange and underwriters would exercise their option for to bring the IPO’s size to about US$25 billion, making it the largest IPO in history.

The political instability in Hong Kong, the frugality measures of the Mainland combined with the stagnant recovery of the Eurozone economy and the Ebola outbreaks in Africa are all potential adverse factors to the financial performance of IPO candidate companies as well as investor confidence. The looming issue of the inevitable increase in the US interest rates will also take a toll in the flow of capital in the Hong Kong markets.

To strengthen competitiveness of Hong Kong’s market in the long run, it is recommended that more interaction in the form of roadshows and delegations between Mainland and Hong Kong are necessary. Hong Kong should also encourage existing issuers to establish new RMB tranches and issue additional RMB shares and expand RMB product offerings and liberalize capital accounts to attract a wider range of market participants.

Shanghai-Hong Kong (SH-HK) Stock Connect, a pilot programme for establishing mutual stock market access between Hong Kong and the Mainland, was launched on 17 November 2014. Investors in Hong Kong and the Mainland can trade and settle shares listed on the other market respectively via the exchange and clearing house in their local market. From a policy standpoint, the SH-HK Stock Connect scheme represents a significant step, among other policy initiatives such as RMB internationalization and Shanghai Free Trade Zone, towards the eventual capital account liberalization in China. From Hong Kong’s perspective, the programme underscores the Central Government’s support of the Hong Kong Stock Exchange, the largest public financing venue for Chinese companies outside of the Mainland. Industry practitioners anticipate that the programme will strengthen the competitiveness of the Hong Kong Stock Exchange and further consolidate the position of Hong Kong as an international financial center. The expanded investment channels available for offshore RMB funds should facilitate an orderly
flow of RMB funds between the two markets represented by the combined daily trading cap of approximately HK$29.6 billion, representing about 20% of the combined daily average trading turnover volume of the two markets combined.\textsuperscript{54}

The Hong Kong Stock Exchange’s US$2.2 billion purchase of the London Metal Exchange (LME) in December 2012\textsuperscript{55} would further enhance Hong Kong’s position to serve the extensive Chinese investment market. China is currently the world’s largest consumer of various resources including coal to copper and zinc\textsuperscript{56} as well as a major producer of base metals. The LME connection with Hong Kong could translate to an all-round development of the local market to offer products beyond traditional equities derivatives trading, to currencies, fixed income and commodities to the Chinese markets.\textsuperscript{57} In 2014, the LME saw the acceptance of its first Chinese-owned broker to trade on its floor\textsuperscript{58} and a Memorandum of Understanding was signed with China Construction Bank Corporation\textsuperscript{59} signaling the increase in the reach of Hong Kong’s financial services to Mainland China.

**Trials Ahead for the Tourism and Retail Sectors**

The tourism and retail industries remain as important pillars of the Hong Kong economy in terms of employment and contribution to GDP. Tourism-related industries employ around 250,000 people and account for 4.7% of Hong Kong’s GDP.\textsuperscript{60} In 2014, both tourism and retail industries faced challenges that may affect growth.

Government statistics showed that visitor arrivals in the first 5 months of 2014 amounted to in excess of 24 million people, representing a 13.6% increase over the comparative figure of 2013. The growth rate of visitor arrivals in 2014 was higher than the corresponding figure of 11.7% in 2013.\textsuperscript{51} The Mainland continued to be the leading source market of Hong Kong tourism, with arrivals increasing by 17.6% from January to May 2014 compared to the same period in 2013. There was a slight increase in the growth of Mainland visitors as compared to the 16.7% overall year-on-year increase in 2013.\textsuperscript{62}

According to research by the Hong Kong Tourism Board (HKTB), in the first 5 months of 2014, short-haul arrivals to Hong Kong increased 6.1% comparing to the same period in 2013, benefiting from the rise of travelers from Korea and Singapore. Overnight arrivals from Korea and Singapore rose 22.1% and 23.9% respectively but there was a decrease of 15.9% in overnight arrivals from Philippines, which could be attributed to the tense diplomatic status between the two places. In addition, overnight arrivals from Indonesia rose 15.5%. As for long-haul markets, there was a slight 0.2% increase in overnight long-haul arrivals to Hong Kong.\textsuperscript{63} New markets such as India, Netherlands and Gulf Cooperation Council countries achieved satisfactory results, with overnight arrivals up 3.7% overall compared to the same period from January to May in 2013.\textsuperscript{54}

Tourist spending accounts for about one-third of retail sales in Hong Kong. The performance of the retail business appeared not to have benefited from the sustained growth in inbound tourism. A 5.5% decrement in value and a 6.4% decrement in volume of retail sales were recorded for the three months ending April 2014.\textsuperscript{65} The total retail sales in April 2014 recorded a further decrease of 9.8% in value and 9.5% in volume over the corresponding periods of 2013. Combining the results of the first four months of 2014, the retail sales registered only a mild increase of 0.7% in value and 1.2% in volume comparing to the same period of 2013. The category of “Jewellery, watches and clocks, and valuable gifts” in April 2014 recorded the highest drop in both sales value and volume. The notable drop was mainly due to the plunge in sales of gold jewellery started in April 2013 which formed a strong comparable base. The outlook for second half of 2014 is full of uncertainties and remain challenging due to slowing down of Mainland tourist’s consumption level and increasing operation cost.\textsuperscript{66} Negative factors including China’s frugality policy measures combined with incidence of protests against Mainland tourists have contributed to the curb in demand for retail sales in Hong Kong, especially for luxury products.

The Individual Visitor Scheme (“IVS”) was introduced in July 2003. While IVS benefitted the Hong Kong economy substantially, it had also created concern amongst the local community regarding the prolific growth of Mainland visitors. In particular, the pressure effect of the IVS on
the public transportation network and shop composition in key districts is evident. Shop floor space rental has been on the rise since 2003 with a surge in shops opening catering to the needs of Mainland visitors with high purchasing power. Some small businesses and those catering to the needs of local consumers were priced out of prime locations. The limited supply of prime retail space coupled with the strong retail sector fuelled by the influx of inbound tourism from the IVS indirectly caused rental rates of retail space to increase 69.4% between 2004 and 2013. The extent of the effect of rising rents is not just prevalent in traditional tourist districts but is diffusing into the local community with recent disputes at residential malls and the New Territories. There is a growing voice in society for Government to strike a balance between the needs of the local community and the growth of the tourism industry in Hong Kong.

In order to attract high-spending visitors to Hong Kong to bring about augmented economic benefits from tourism, there is a need to continue to upgrade tourist facilities, maintain an adequate supply of high-end hotel accommodation and host attractive mega events. On tourist facilities, the construction of the waterpark at Tai Shue Wan in the Ocean Park has commenced and discussion on phase two development of the Hong Kong Disneyland was announced in the 2015 Policy Address. The terminal building and the first berth of the Kai Tak Cruise Terminal came into operation in June 2013 and the second berth entered service in September 2014. Amongst other attractions, these new developments will enhance Hong Kong’s diversity and appeal to visitors.

On the accommodation front, Government is pressing ahead with the infrastructure works at the southern end of the runway and south apron of the former Kai Tak Airport. Feasible ways are being identified for the gradual release of the six sites facing Victoria Harbour within the “hotel belt” adjacent to the Kai Tak Cruise Terminal to the market starting from the end of 2015. This prime site could potentially be developed into a distinctive hotel cluster to alleviate the short supply of quality tourist accommodation in Hong Kong as well as enhance the development of the area. The hotel project at the Murray Building site has been successfully tendered. The increase in supply for hotel rooms will provide more diverse and unique choices of quality accommodation to support the vibrant tourism industry.

According to the HKTB, visitors attending conventions and exhibitions in Hong Kong spent HK$16.3 billion in 2013. The convention visitor’s average per capita spending was close to HK$10,000, representing 21% premium over other overnight visitors. In response, HKTB will allocate HK$45 million from Government to provide targeted services and concessions for organisers and participants of conventions and exhibitions of various scales and types from 2014 to 2017. Meanwhile, Government is studying the demand for convention and exhibition facilities in Hong Kong for the next 15 years in view of affirmative action to enhance capabilities in the area. In the 2015 Policy Address, Government announced plans for constructing a new convention centre above the Exhibition Station of the Shatin to Central MTR link. Additional funding of HK$50 million from Government will be provided to the HKTB in 2015 and 2016 to strengthen and further promote popular cultural, art and sports events. Government will continue to seek opportunities to host mega events with financial support from the Mega Events Fund. Events such as Hong Kong Sevens, Hong Kong Dragon Boat Carnival, and Hong Kong Wine & Dine Month, could refresh Hong Kong’s appeal to overseas visitors and attract them to come back again at different times of the year.

Nevertheless, the Occupy Central movement, lasting for 79 days from 26 September to 15 December 2014, had inevitably negatively affected both retail and tourism industries. During this period, the Central Government had appeared to suspend travel permits for Mainland tour groups to Hong Kong, which could materially affect the performance of both industries. With key tourist areas such as Causeway Bay, Mong Kok and Central being affected and traffic paralysis resulting in the demonstrations, retail sales in affected areas were reported to have lost business volume of up to 70% in the traditional National Day golden week. The number of inbound tour groups registered by the Travel Industry Council of Hong Kong dropped by 30% over the seven-day National Day holiday leading to concerns of the downturn in tourist arrivals and its long term consequences. It was further proclaimed that the whole industry was losing at least HK$50 million each day. Although the Occupy Central movement has come to end, the pro-democracy protest has taken into a new form known as “shopping tour” with activists gathering on footpaths to window-shop, which may continue to disrupt retail businesses and effect tourism.
Maintaining Competitive Advantage in the Logistic Industry

Hong Kong is renowned as an international and regional logistic hub due to its strategic geographical location, well-developed infrastructure and free-port status. The logistics and trade industry is one of the four pillars supporting Hong Kong’s economy, which accounts for around 25% of its GDP and employs over 700,000 people. According to the Census and Statistics Department, the growth in volume of trade continued to decline in the first quarter of 2014. In terms of value of trade, imports recorded a year-on-year growth of 2.7% in April 2014. Total exports registered a continued yet modest increase of 2%, in which domestic exports fell by 6.7% and re-exports rose by 2.2%. Total container throughput grew by 2.5% and air freight throughput increased by 5.6%.

In terms of capacity of processed cargo, Hong Kong continues to lose out to Singapore and Shanghai while its competition with Shenzhen remains intense. In 2013, Shanghai remained as the world’s busiest port with Singapore trailing closely behind, Hong Kong plunged to fourth place with Shenzhen overtaking its previous position. In the first half of 2014, Shanghai handled cargo throughput of 17.26 million TEU. Singapore recorded a total throughput of 16.51 million TEU. The corresponding figure for Shenzhen was 10.98 million TEU compared with 11.2 million TEU in Hong Kong indicating a resurgence of Hong Kong’s position.

With a world class international airport, Hong Kong has an advantage in airfreight logistics. Since 2010, it has registered the world’s largest air cargo throughput. To maintain its competitive strength, the Third Runway Project is in the pipeline to boost volume of cargo throughput. In September 2014, the Advisory Council on the Environment endorsed the Airport Authority’s environmental impact assessment report on the Project. The consensus was that while the construction of the third runway or any other works in the area would effect the wildlife and environment, the extent of the effect could be mitigated. Hong Kong International Airport’s passenger volume hit a record 56.5 million in 2013, while the number of flight movements rose 5.3% from 2012 figures to 352,000 flights, indicating the urgent need for a third runway. A third runway would be able to handle a practical maximum capacity of 620,000 flight movements per year. This would meet and go beyond the traffic demand forecast of 602,000 in 2030. It is anticipated that the alternate plans to increase the investment in existing terminal and apron facilities to expand capacity would only increase the practical maximum capacity of 420,000 flight movements per year and meet the estimated demand for air services in the medium term. Hence it is of utmost importance to commence development of the third runway to maintain Hong Kong’s competitiveness as an airfreight logistics hub. Based on the preliminary master plan of the Airport Authority, the cost of the project is expected to reach HK$136 billion and be completed by the year 2023.

The logistic industry has expressed a more conservative attitude towards the Container Terminal 10 (CT10) Project. The CT10 Project was put forward 10 years ago due to a projected annual growth of 10% of cargo volume in Hong Kong. The growth in cargo volume is revised to drop between 1% to 3% from 2020 indicating a less pressing need to pursue the project. The expected rate of return of the CT10 Project also raised concerns. At an estimated construction cost of around HK$100 billion, a return of 10% to 12% would be required to justify private investment, but analysis had penned economical return at 4% for the project. Instead, a better use of existing facilities can boost port capacity by 15% with a spending on just 40% of the construction cost. In the meantime, studies on the technical feasibility and environment impact are still being carried out but the momentum of the project suggests that the plan would not reach the construction stage for the near future.

The issue of a limited land supply for logistic use poses a difficulty for the industry. Land is required for distribution centres, logistic parks and warehouses to support growth of the industry. Land supply has traditionally been an issue in Hong Kong. High rent of warehouses has continued to increase service providers’ operating costs. The vacancy rate of warehouses is at less than 1%, and rent is expected to sustain a 5% to 10% growth in 2014. In response to the land shortage issue, Government has released three logistics sites with a total floor area of 280,000 square meters at Tsing Yi since 2012. The sites were tendered with the specific usage for logistics development purposes and would be nearing completion in the fourth quarter for 2014. Government has also set aside 10 hectares of land at Tuen Mun West Area 38 and Area 49 for the development of the logistics industry. Further parcels of land in Tuen Mun Area 40 and 46 are
planned for industrial or logistic uses. The new land sites are strategically selected to be near the in-construction Tuen Mun-Chek Lap Kwok Link and Tuen Mun West Bypass highway scheduled for completion in 2018, making the sites easily accessible to the airport and border. It is anticipated that the new injection in land supply designated for logistics use will enhance the development of the industry.

Nevertheless, logistics operations faces the imminent problem of labour shortage of skilled workers and management expertise. With the Hong Kong economy at near full employment and the logistics industry being perceived as labour intensive with limited prospects, there are difficulties in attracting new entrants to the industry. The lack of formal and in-house training programmes to develop talent in the logistics industry is another reason why the industry faces a shortage of skilled manpower. Industry analysis expressed that the shortage of skilled management expertise of the industry has caused the proportion of costs allocated to logistics management to be higher in the Hong Kong market compared to that of the US. This in turn is indicative of an inefficiency of the local logistic sector. In order to maintain the competitive advantage of the Hong Kong logistics industry, the issue of labour supply must be addressed.

In response to the challenges facing the logistic industry, in the 2015 Policy Address, Government announced plans to enhance the functions of the Hong Kong Maritime Industry Council and a new maritime body will be established to enhance Hong Kong’s competitiveness in the marine industry. Concurrently, the newly established Maritime and Aviation Training Fund will help expand the pool of talent for the industry to alleviate the labour shortage issue.

**Developments of Mainland Special Economic Zones**

Special Economic Zones of Mainland China refers to the specified locations which are mandated to have special economic policies such as tax concessions, lifting of certain legal restrictions or even subsidies for foreign investments. In general, the zones are established to facilitate for immediate developments of certain geographical areas or industries. In 2014 three special economic zones are of particular concern in terms of opportunities and competition to Hong Kong.

**Developments in Hengqin**

Hengqin is an island in Zhuhai, China in close proximity to Macau. In 2009 parts of Hengqin was leased to Macau by the State Council of China. In accordance to China’s 12th Five Year development plan, Hengqin in Zhuhai is a key strategic development area in the Pearl River Delta of Southern China. Hengqin intends to attract investments from leisure and tourism, financial, modern logistics, cultural innovation, medical and technology sectors. Hengqin’s size of approximately three times of Macau and a bridge links the two destinations. Its close proximity to the vibrant gaming city and availability of undeveloped land resources indicate that Hengqin’s development would be complementary to Macau. From January to August 2014, 21 million cumulative visitors passed through Hengqin to access Macau. Hengqin’s latent ability to serve as a tourism support hub for Macau is proven.

In September 2014, University of Macau’s new campus on Hengqin Island commenced partial operations. The additional space and facilities for the campus is anticipated to develop much needed quality human capital for Macau and Hengqin. The anticipated opening of Chimelong Ocean Kingdom, the world’s largest aquarium and water theme park took place in March 2014. The aquatic theme park was built with investment of over US$806.5 million and had attracted in excess of 5 million tourists as of September 2014.

By the end of May 2014, a mere 79 Hong Kong enterprises out of a total number of 5,300 companies had incorporated in the Hengqin Area. This indicates that Hong Kong businesses are still skeptical on investing in Hengqin. It is anticipated that with the near completion of the first phases of infrastructure and investment projects, Hong Kong businesses would be incentivized to invest in Hengqin. As of the end of 2013, a total of RMB 44 billion was spent on infrastructure projects to provide electricity, water and sewage facilities to the newly developed areas of Hengqin. Companies incorporated in Hengqin under prescribed sectors are subject to a concessionary Corporate Income Tax rate of 15% as compared to the national rate of 25%. The strong tax incentive serves as an additional reason for Hong Kong businesses to invest in the area.
Several Hong Kong companies have publicly indicated interest on plans to build large tourist attractions in the region. In order to promote investment through capital financing, the state owned Hengqin Financial Investment Co Ltd was established in May 2014, to support development in the area. The firm has signed US$3.25 billion worth of cooperation agreements with potential investors since its establishment up to September 2014.

The opportunity for Hong Kong businesses to be involved in Hengqin’s development would be enhanced by the anticipated completion of the Hong Kong-Zhuhai-Macau Bridge in 2016/17. At that time travelling to Hengqin from Hong Kong would take less than one hour. Through enhanced accessibility, there are promising prospects for Hong Kong’s professionals, service providers and retailers to consider investment in Hengqin’s dynamic environment.

Developments of Qianhai

The Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone is another key strategic development area in the Pearl River Delta of Southern China. Located at the west of Shekou Peninsula near the Shenzhen Bay Port, Qianhai is in closer proximity to Hong Kong in comparison to Hengqin. Upon completion of the Hong Kong-Guangzhou Western Express Railway in 2017, Qianhai would be approximately 10 minutes away from the Hong Kong International Airport, 7 minutes from the Shenzhen airport, and 30 minutes away from Central, Hong Kong by high speed train. The area of Qianhai covers around 15 square kilometers and construction of infrastructure was scheduled to be completed by 2020.

The key industrial focus of Qianhai includes financial services with cross-border Renminbi lending measures, modern logistics and information technology. In 2014, the major policy developments of Qianhai are relatively similar to Hengqin in terms of tax concessions for companies incorporated there as well as an income tax break for foreign professionals working in the development zone. In 2013/14 the Shenzhen Municipal Government mandated to heavily invest in the infrastructure works in Qianhai to the tune of US$1.59 billion in 2013. This has attracted a positive response from potential investors. As of August 2014, up to 12,902 companies were incorporated in Qianhai of which 8,284 companies are from the finance industry representing a 12.6% increase to the corresponding incorporation figures of 2013. The results of public auction for land in Qianhai were extremely positive, with top tier companies like China Resources Group and Tencent Holding Ltd purchasing prime real estate in the area.

In January 2014, the British Virgin Islands signed a preliminary Memorandum of Understanding with the Qianhai authorities to boost investment across four sectors in the region on finance, logistics, information technology and professional services. It is anticipated that Qianhai would be a test bed for China’s currency liberalization and financial reforms within the Mainland and foreign investment would play an increasingly important role its development. Market commentators indicated that the Qianhai zone has a much larger purpose than previous economic zones and its success could be a major turning point in China’s increasingly urgent momentum to liberalize its economy and loosen its monetary policy.

With the proximity of Hong Kong and Qianhai, there are abundant opportunities for local businesses to benefit from the special concessions of the development zone as a portal for investment into the Chinese capital markets. In terms of competition from the region as a finance center, the legal system and regulators of the Mainland are still relatively fragile in comparison to Hong Kong hence the direct competition from the region will be a longer-term problem.

Developments in the China (Shanghai) Pilot Free-Trade Zone

The China (Shanghai) Pilot Free-Trade Zone (SFTZ) was launched on September 29, 2013. The entire zone covers a combined 28.78 square kilometers, and is a confluence of four existing bonded zones including the Waigaoqiao Free Trade Zone, Waigaoqiao Free Trade Logistics Park, Yangshan Free Trade Port Area and Pudong Airport Comprehensive Free Trade Zone. The physical locations of the zones are scattered around the Shanghai region and are not in a single location.

The much anticipated zone was lauded by Mainland government officials to be a landmark achievement, similar to the creation of the Shenzhen special economic zone that would bring reforms and was supposedly an unprecedented development in the history of China. Contrarily
at launch the authorities released a “negative list” of sectors containing over 1,000 banned areas in which foreigners cannot invest in the zone. Combined with unclear information as to the exact benefits of the zone and limited change in the banking, trade and tax policies, critics have panned the zone as a disappointment due to lack of progress on promised financial deregulation. Apart from the geographical proximity to Chinese consumers, many foreign investors seemed ignorant about the benefits of operating in the zone. Media reports and commentary had suggested that although a number of companies were attracted to incorporate in the zone, their progress after registration was limited. The zone seemed to be focusing on easier and less crucial reforms such as the relaxing restrictions on merchandise trade rather than genuine free trade as the name of the zone suggested.

As of June 2014, newly registered foreign companies represented only 12% of 10,000 firms operating in the zone and foreign companies based outside of Hong Kong and Taiwan accounted for a mere 6% indicating that the zone had not successfully attracted sufficient foreign investment. This lackluster development and unclear positioning of the zone translate to the idea that the SFTZ does not pose a threat to the competitiveness of Hong Kong as a truly free market and international hub for trading and investment. Although due attention should be paid to the developments and policy changes within the zone in the future as the establishment of the zone could be interpreted as a slow commencement step for China to liberalize its trade and foreign exchange policies.

**Welcoming the Dawn of Big Data Analytics**

In the 2014 Conference Board CEO Challenge Survey, big data analytics was identified by over 1,000 top executives from around the world as the most important hot button issue. Big data analytics refers to the process of collecting, organizing and analyzing large sets of data to discover patterns and other useful information. In a business application this would involve understanding the information collected and translating it into useful indicators to base business decisions or enhance operations.

Modern communications technology dictates business operations of all services and industries. The average consumer now has around the clock access to an active internet connection by way of a mobile device or computer. In Hong Kong, the estimated number of internet users is at 5.75 million representing an overall penetration rate of 73% of the population. An increasing majority of consumers are receiving and disseminating information via social media revealing their preferences, social circles and lifestyles into the public domain. As of the first quarter of 2014, the world’s premier social media network Facebook had 1.28 billion monthly active users. To most people these records may be classified as junk data but deriving value out of the huge volumes of data created by internet users on a day-to-day basis has become commercialized by companies like Google and Facebook that are increasingly applying analytics and decision making solutions to capture, manage and process data.

Big data analytics allows companies to benefit from real-time market intelligence. As an example, an individual’s preferences, expenditure pattern and demographics could be deduced through analysis of data from online location, browsing history and social media behavior. The available software technology can automatically analyze patterns from these seemingly junk data to provide individualized advertisements to enhance the success rate of sales through direct marketing thereby increasing revenues. This could allow companies to obtain a competitive advantage by discovery of trends and characteristics about their customers that might otherwise remain hidden and concentrate on marketing for target customers to achieve cost savings. This is one of many examples of how big data analytics could enhance businesses.

There are however, also costs associated with establishing, maintaining, collecting and analysis of consumer data and smaller companies may not have the resources or scale to fully benefit from big data analytics. It is documented that the SME adoption rate of big data analytics is extremely low.
in the United Kingdom. SMEs in Hong Kong that are facing similar budgetary concerns may similarly lack the resources to engage and benefit from big data analytics.

In Hong Kong, big data analytics is still a relatively novel concept in the business community. At the Big Data and Business Analytics Forum 2014 held in Hong Kong, speakers shared the view that there appears to be a gap in big data development between Mainland China and Hong Kong let alone the International stage. While Hong Kong is perceived as more technologically advanced than the Mainland, there are limitations as to the uses of big data analytics due to the demographics. As the total population of Hong Kong is relatively small, the unit costs for collecting big data will inevitably be higher than the Mainland and other economies with a larger population. Hong Kong businesses are seemingly skeptical on the investment necessary for big data and the pure fact that executives are still unclear on what benefits big data analytics could bring to their business.

The big data market is still at an emerging stage and is expected to experience rapid and augmented development as organizations seek to enhance their competitive advantage. The Hong Kong business community should remain diligent on this new tool in business. Big data analytics is consequently an opportunity and tool for businesses to gain a deeper insight into whom their customers are as well as to anticipate demand and enhance its product offerings accordingly. This key to consumer’s mindset can in theory and practice change the whole approach to doing business in the near future.

2. SOCIAL FACTORS

Manpower Shortages at Full Employment

The quality and quantity of the workforce is a key determinant of an economy’s growth potential. With limited natural resources, the continuous growth and prosperity of Hong Kong is dependent on human capital. The unemployment rate of Hong Kong stood at 3.3% in September 2014. This figure suggests that Hong Kong is at near full employment. Many industries are finding it difficult to find suitable manpower to fill openings especially in the skilled labour and intensive industries. A Report on Manpower Projection to 2018 released by the Legislative Council in April 2014 predicted that Hong Kong would face a labour shortage by 2018 with a vacuum of 22,000 workers with higher education and 14,000 workers across every education level. As Hong Kong’s economy is knowledge based, the statistics of a shortage of educated workers bids for immediate concern.

Labour shortages in multiple industries were reported in 2014. HAECO, the aircraft maintenance magnate reported that it had a labour shortage of 1,000 openings which is effecting its bottom line. The Hong Kong Retail Management Association reported 7,900 unfilled vacancies in the retail sector. Representatives of the property management industry estimated a shortage of up to 17,000 workers in the industry. Similar concerns were raised by the Elderly Services Association of Hong Kong proclaiming the need of 5,000 staff on top of the 20,000 already working in the field. The Federation of Restaurants and Related Trades, claimed the food services industry was in need of 24,000 workers on top of the 240,000 employed now. It is estimated that there are up to a shortage of 10,000 skilled construction workers in Hong Kong, particularly in steel reinforcing, scaffolding, and nail-plating, where workers with the necessary skill-sets are usually over 50 years old and due to the labour intensive and harsh working environment, there are few new entrants of younger labourers to the industry.

Government has a Supplementary Labour Scheme which allows employers with “genuine difficulties” finding suitable local staff to import workers. However only a mere 2,612 foreigners were admitted up to June 2014 suggesting that the scheme is not sufficient to fill the void in the supply of labour. Although Government made plans to relax the vetting procedures of the scheme, the situation remained that imported workers accounted for only 0.1% of Hong Kong’s labour force, compared with 26% in Macau and 28% in Singapore. The high property prices and domestic rental rates translating to costs and availability of living space for imported labour poses a practical problem on the importation of labour. Furthermore, unions and a number of political parties held opposing views to importation of labour. It is anticipated that any subsequent legislation regarding importation of labour in Hong Kong would be met with
opposition. In the 2015 Policy Address, Government announced the enhancement of the Supplementary Labour Scheme for the construction industry to ensure the industry’s productivity and competitiveness is not adversely affected by the labour shortage issue at hand.

Minimum wage has been implemented since May 2011, the current rate of HK$30 per hour was set in May 2013. There are views that the implementation of minimum wages has enhanced the manpower shortage problem in certain industries employing workers with lower technical skills and hard manual labour. As the lowest wage level is statutorily determined workers would seek jobs with better working conditions at the same pay. This has caused an imbalance of labour supply to differing minimum wage positions available. Certain minimum wage job openings remain unfilled while others are in high demand. This irregularity has driven wage for certain labour intensive jobs upwards adding to costs pressure for businesses. Minimum wages may also decrease the labour force participation rate as the public housing income and assets limit criteria state the maximum income limit per month for a family of two persons is HK$14,970. If both persons worked at the minimum wage their combined monthly income could exceed the income limit depending on hours worked. Hence workers applying for public housing may work part time or at an underemployed capacity in order to be eligible for subsidized homes boosting the shortage of labour issue.

The consultation on standard working hours added potential pressure to the labour market. From employer’s perspective stipulating standard working hours would mean more staff may need to be hired to ensure compliance with working hours or high overtime costs would be incurred. Workers and trade unions supported standard working hours as a protection to employee rights. However, under a situation of near full employment and labour shortage the implementation of such policies would place cost pressures on businesses and may adversely affect the competitiveness of Hong Kong’s products and services. Although still at a consultation stage, the prospective implementation of standard working hours poses an impending challenge to the Hong Kong labour market.

As the population ages, a sustainable manpower supply for future development is needed. Alternate solutions are found in the extension of the retirement age and the targeted engagement of certain demographic groups with a comparatively lower labour force participation rate. In the 2015 Policy Address, Government announced the extension of retirement age for civil servants. With no mandatory retirement age in Hong Kong, organizations and the business community are free to provide incentives to extend employment for senior citizen staff members and recruit retired staff at their discretion. Practical issues such as skills mismatch, physical ability and statutory employee compensation insurance are additional challenges to recruiting retirees. Employers raised concerns that the higher insurance premiums for older employees would increase operating costs. Industries that require registration of practitioners such as property management have age restrictions. As an example security guards aged over 65 may only work at single building properties meaning that many able workers are forced to retire as their scope of service are legally limited once they reach a certain age.

On the other spectrum of the age range, younger demographic groups recorded a higher unemployment rate and lower labour force participation rate. For 2013, the 15–19 year old age range has an average labour force participation rate of 11.25% and the 20-24 year old range has a corresponding figure of 63.35%. The unemployment statistics from July to August 2014 illustrate that the 15–19 year old age range unemployment rate was at 12.7% and the 20-29 year old range corresponding figure was at 7% which are considerably higher than the overall rate of 3.3%. This suggests that there is a potential underappreciated labour supply in the younger spectrum of the working population that is not fully recognized by employers.

There are several key corresponding initiatives delivered in the 2014 Policy Address on Vocational Training and Manpower Development to enhance the employability of the younger segment and under employed groups. For instance, funding Vocational Training Council to implement the pilot traineeship scheme in services industries which aims to provide young people aged 15 or above with in-service training and relevant vocational education. The scheme is anticipated to expand its coverage from the existing beauty care and hairdressing industries to other services industries, including the elderly care services industry. In addition, this initiative promotes the employment of young school leavers through providing enhanced on-the-job training allowance to employers.
For groups with lower labour force participation rates, Government is taking a dual approach to encourage employment in both the public and private sector. The recruitment formats for civil servant positions would be reviewed to enable equal access and opportunities for ethnic minorities, women and disabled persons to join the public sector. For the private sector, the Labour Department job centers established special referral services for job matching. Job fairs and special training courses would be arranged for these groups with lower participation to enhance their chances of employment. Specific initiatives to help the individual groups could be found. Construction Industry Council (CIC) has proactively sought minorities’ entrants into the short staffed construction industry. The Selective Placement Division of the Labour Department provides free specialized employment assistance to persons with disabilities.

During 2013, the programme achieved 2,461 placements. The Labour Department also administers the Work Orientation and Placement Scheme which encourages employers to offer job vacancies to persons with disabilities through the provision of allowance. To encourage women with dependent children joining the workforce the Social Welfare Department would allocate additional resources in 2014/15 to extend the service hours in some after-school care centres under the Neighbourhood Support Childcare Project. By enhancing the employability and participation rate of these groups, it is hoped that the manpower shortage issue could partially be alleviated. To enhance employability of new arrivals and ethnic minorities, Government announced the provision of 1,300 and 800 training places through the Employee’s Retraining Board in the 2015 Policy Address.

Affirmative Action for Poverty Alleviation

A poverty line was set in September 2013 by Government with the concept of relative poverty in mind and is determined to be at half of the monthly median household income. This is a welcoming change and a positive step in the direction to address the poverty issue as the situation of the wealth gap is at an elevated level. The last published Gini Coefficient Index measuring the poverty gap has reached 0.537, which is the highest figure of any developed economy, according to World Bank research. It is anticipated that, once a poverty line was drawn, there is bound to be greater pressure exerted on Government to introduce more initiatives for poverty alleviation.

The median monthly income for all Hong Kong households in the second quarter of 2014 was HK$22,900 for a family of around 2.9 persons. A family of three with a monthly income of less than around HK$11,550 would be below the city’s poverty line. This effectively suggests 19.6% or roughly one in five person in Hong Kong’s population is living below the poverty line which would be an over estimate by most purposes. According to corresponding statistics released in June 2014, 6% of all households in Hong Kong live with a monthly income of below HK$4,000 and a total of 21.2% live with a monthly income of below HK$9,999. This indicates that even in relative terms a substantial portion of the population is defined as poor due to the nature of the disproportionate income distribution of Hong Kong.

In the 2014 Policy Address, the Chief Executive stated that the poverty line provided a clear and objective basis to review the poverty situation, formulate policies and assess the effectiveness of measures. Building from this positive identification of problems, multiple affirmative action initiatives were launched to address the poverty situation. Government is shifting from the approach of relying on one-off handouts and short-term subsidies to establishing a system to help low-income working families to encourage self-reliance and continual participation in the labour market and achieving direly needed wealth equality without reliance on transfer payments of benefits.

The highlight of the new initiatives is the HK$3 billion-a-year plan for a Low-income Working Families’ Allowance assisting non-Comprehensive Social Security Assistance (non-CSSA) working families living below or slightly above the poverty line, especially those with children at school. More than 200,000 low-income families with 710,000 members, including 180,000 eligible children and young people, will benefit from the allowance. As the basis of this allowance is tied to employment income and eligible only for families whom are not on benefits it can effectively encourage continued employment and offer assistance to families that are trying to avoid poverty through their own means. The two-tier allowance is based on working hours and family income and the full basic allowance of HK$600 or HK$1,000 per month depending on the working hour...
tier to which it belongs. If the family includes children or youth members, it is entitled to an additional full allowance of HK$800 per month for each eligible child or youth member to ensure that the second generations have more resources and opportunities to break the vicious cycle of inter-generational poverty. This affirmative initiative will be implemented in 2015 and is widely welcomed by social welfare organizations.207

Concurrently, Government has announced that the Community Care Fund will receive HK$10 billion in 2014-15 and donations from the business sector. The Fund has launched a total of 18 programmes to offer appropriate assistance to over 100,000 people in need, including those not covered by Government's safety net. The Commission on Poverty could use the injection to alleviate poverty by enhancing the reach of the social welfare system to programmes that have proved to be effective but have yet to be incorporated into the Government's regular assistance and service programmes. In the 2015 Policy Address, Government further earmarked HK$ 50 billion for retirement protection of needy citizens.

The business community’s involvement in poverty alleviation has been steered by Government’s initiatives. The Social Engagement Task Force was established under the Commission on Poverty in February 2013 to engage the business community on dealing with poverty. The Bless Hong Kong Campaign was launched by the task force in February 2014 to facilitate for the tripartite partnership of Government, businesses and the general public on poverty alleviation efforts. In excess of 250 social welfare organizations and companies were partner organizations of the scheme. Initiatives in 2014 was highlighted by the Future Stars programme in which businesses were encouraged to give employment opportunities, skills training, internships and scholarships to underprivileged youths. The programme aimed to boost upward mobility of underprivileged youths and to bestow opportunities and vocational knowledge to enhance employability.

In light of the close to full employment situation in Hong Kong, Government’s policies and the business sector’s efforts to improve wealth distribution and alleviate poverty is pragmatic and does not discourage people from working by expanding the base of pure financial assistance. The initiatives directive of helping people help themselves appear to be the direction for poverty alleviation.

Consultation on Voluntary Private Health Insurance Scheme

Government's recurrent expenditure on medical and health services increased from HK$32 billion in 2007-08 by over 60% to the budgeted expenditure of HK$52 billion in 2014-15. Public Health expenditure accounts for about 17% of Government’s total recurrent expenditure. Under the situation of an ageing population, shortage of medical professionals, increasing costs of provision of healthcare services and a rise in demand, the public healthcare services will inevitably be operating under stress in the near future.

In December 2014, Government commenced the consultation on the Voluntary Private Health Insurance Scheme. The aim of the scheme is to alleviate the pressure on the demand for public health services by providing financial incentives for usage of private healthcare facilities, thereby adjusting the balance of public-private healthcare sectors. It is anticipated that users of public healthcare services can benefit from shorter waiting time and enhanced service quality with the diversion of consumers to the private sector. Features of the proposed scheme state that personal health insurance schemes with hospital indemnity clauses must provide a standard plan that comply with 12 Minimum Requirements prescribed by Government to ensure standardized coverage, accessibility and consumer equality. The proposed scheme differentiates itself from existing insurance products as Government will extend coverage for medical procedures not usually covered by insurance and introduce fixed premiums even when a user’s health deteriorates. Government will publicly fund HK$ 4.3 billion into a High Risk Pool to enable individuals deemed to have higher health risks to have access to insurance schemes for a 25-year period starting from 2016 to 2040. Due to the wider intended coverage the proposed insurance scheme would be approximately 9% more expensive than the current corresponding market products with a yearly premium of approximately HK$ 3,600. Government anticipates that the increase in premiums could be offset by tax deductions and rebates to provide incentives for purchasers.
In the long run, it is expected that the scheme will contribute to the sustainable development of Hong Kong’s healthcare system. A balance in demand could enable the private and public healthcare sector to complement each other to enhance the efficiency of the medical services sector of Hong Kong.

**Land Supply for Housing and Commercial Development**

Hong Kong’s residential property market has risen relentlessly for four years since 2010, and the problem is causing political issues and social unrest.\(^{217}\) Government tried to cool the property market through many instruments such as higher stamp duties for expensive properties and extra stamp duty for properties resold within a short period of time, imposing extra stamp duties on foreign buyers as well as doubling stamp duties for certain properties.\(^{218}\) The measures successfully curtailed the number of property transactions but the effect on house prices was marginal. The solution to the problem therefore would appear to be on the supply side. In the 2014 Policy Address, the Chief Executive acknowledged that serious housing shortage is at the core of the problem of the housing market and developing new land and increasing housing supply would be the desired solution.\(^{219}\)

The issue of an overheating property market and a mismatch of demand and supply have caused the problem at hand. Since 2010, Government has sought to coordinate and spearhead efforts in expanding land resources for housing development.\(^{220}\) Government has subsequently identified about 80 additional Green Belt sites and Government, Institution or Community sites in various districts with a total area of over 150 hectares with the potential to be rezoned for residential use. There are about 150 sites that have to be rezoned for residential use and will be made available over the next five years from 2014 to provide about 210,000 additional public and private housing units.\(^{221}\) Government simultaneously explored various measures to increase housing land supply, including the redevelopment of aged Public Rental Housing estates; large scale reclamation of land in prime locations; the Tung Chung New Town extension; Lantau development and establishment of New Development Areas. These possible solutions were mentioned in the Long Term Housing Strategy Steering Committee consultation report.\(^{222}\) In December 2014, the revised target of Government was to increase housing supply to 480,000 new residential units by 2025, with public housing accounting for 60% of the supply.\(^{223}\) There were concerns over whether Government had sufficient suitable land supply in the Land Sales Programme to achieve the rather high supply target.\(^{224}\) Concurrently, Government announced that a housing reserve would be created to help the Housing Authority reach the public flat construction target. Government surplus would fund the housing reserve with an initial transfer of HK$ 27 billion to be made in 2015.\(^{225}\)

New Development Areas (NDAs) would provide a good source of land supply in the medium to long term. Public housing in NDAs could potentially reduce the waiting time for this sought after provision\(^{226}\) as with the new towns developments in the 1960s to 1980s such as Tsuen Wan, Sha Tin, Tai Po, Tseung Kwan O, Tin Shui Wai, Tung Chung and Tuen Mun that significantly increased public housing supply.\(^{227}\) The greatly contested North East New Territories New Development Area (NTNENDA) would add to the land supply and potentially alleviate the property situation at hand.\(^{228}\) The NTNENDA is anticipated to provide an additional supply of 60,700 residential flats for 170,000 new residents in the first phase located at Kwu Tung North and Fanling North with Ping Che under review for re-planning.\(^{229}\) Nevertheless, the NTNENDA plan was met with unyielding opposition from a wide array of effected local residents, environmentalists, as well as opposition groups with no direct vested interest. Discontent on the plan was thoroughly expressed in the form of heated protests and media criticism of both genuine and frivolous concerns.\(^{230}\) Disputes arising from the development plan ranged from displacement to compensation, to conflict of interest of Government officials and environmental concerns.\(^{231}\) Amongst opposition voices were views that purported that the NTNENDA plan with 60% public housing and 40% private market supply\(^{232}\) would be a transfer of land resources for the benefit of private property developers as well as a plan to sell-out the New Territories North region as a “back garden” for the affluent Mainlanders in future or turn the region into an “extension of Shenzhen” or “grey imports and smuggling town” to exclusively serve Mainland tourists.\(^{233}\) Although the NTNENDA plan finally received a tight vote of approval and initial funding of HK$ 320 million, it clearly illustrates the difficulty Government is facing in attempt to increase land supplies without full support of its citizens. To further boost land supply, in the 2015 Policy Address, Government announced plans for developing “brownfield sites” in Hung Shui Kiu, Yuen
Long South and New Territories North and taking forward the development of Lantau Island such as Tung Chung New Town Extension.

Besides boosting land supply to facilitate housing development, Government has been planning to support Hong Kong’s long-term economic development through expanding or rezoning land supply for commercial use. The Energizing Kowloon East initiative is among the most concerned project. It aims at facilitating the development of Kowloon East into a new Central Business District (CBD). Since 2001, all industrial land in Kwun Tong and Kowloon Bay was rezoned to "Business" use which would allow industrial premises converted to office use and industrial buildings redeveloped for office and commercial uses. By the end of May 2012, 48 applications have been approved for wholesale conversion or redevelopment and 23 of them are in Kwun Tong and Kowloon Bay. These industrial buildings will be redeveloped or converted into offices, shops and services, and hotels in line with the changing economic environment of Hong Kong. At the same time, Government is giving more consideration to arts and cultural community and creative industries in its land supply and zoning policy.

Part of the Kowloon East initiatives comprises of the 320 hectare Kai Tak Development Area, (KTDA) which includes approximately 1.06 million square meters of office space; 0.8 million square meters of retail and hotel accommodation; and some 33,200 public and private housing units. With the cruise terminal, sports and tourism facilities, KTDA will inject development density and diversity into the area that was previously Hong Kong’s airport. Together with the emerging Kwun Tong and Kowloon Bay Business Areas, Kowloon East would evolve into a vibrant premier district of Hong Kong.

Providing Skills for a Knowledge Based Economy: The Continuing Education Market

Continuing education is considered as a lifelong process for people of all ages to acquire knowledge and skills, which are critical assets for individuals and businesses alike. Under the situation of near full employment and a highly mobile labour market, the prominence of continuing education is gaining sound momentum. Individuals and organizations are more readily willing to equip themselves and their staff with new skills and knowledge through continuous education.

According to a report published by the Caritas Institute of Higher Education, there are approximately 70,000 secondary school graduates each year in Hong Kong, yet there are only around 16,000 undergraduate degree admissions to the eight recognized Universities. In order to secure a fitting career path and delay entrance into the labour market, most of these fresh school graduates choose alternative study paths. Evidently the labour force participation rate for males 15-19 years declined from 34.5% in 1986 to 17.1% in 2001 to 10.5% in 2012 and for females the decline was from 31.7% in 1986 to 15.5% in 2001 to 9.7% in 2012. The gradual decline in the labour force participation rate at younger age ranges is the byproduct of an advancing knowledge based economy like Hong Kong. As new entrants to the labour market with the necessary skills and knowledge are direly needed, the supply of quality continuing education programmes is the key to maintaining a vigorous workforce for our knowledge based economy.

In 2013 there were about 69,800 graduates from HKDSE and approximately 22,360 Bachelor’s Degree programmes spaces offered by 17 continuing education organizations in Hong Kong. A further 39,500 places of Sub-Degree programmes were offered by 23 institutes. There were also around 11,300 places in Diploma programmes offered by various local institutes. Thus, HKDSE graduates and school leavers are well catered for by continuous education providers to gain the necessary knowledge and skills.

Looking at statistics of demand for continuing education amongst adults in the age of 18 - 65 in Hong Kong, the participation rate of continuing education programmes could be extrapolated from the number of applications to the Continuing Education Fund (CEF) Scheme. Under the CEF Scheme, adults in the age range will be subsidized for continuing education and training courses through reimbursement of up to 80% of course fees, subject to a maximum sum of HK$10,000 per applicant, on successful completion of a reimbursable course. As of August 2014, merely 733,709 cumulative applications were received compared to the corresponding population...
of 4,507,500 persons for the 25-64 age group. Given the fact that the age range data excluded the lower and top end of the population and not all continuing education courses were CEF accredited, the application data indicated that there is still a positive growth margin of the continuing education market in Hong Kong.

In a survey report from the Journal of Youth Studies, participants indicated that the top obstacle in attaining continuing education was “no time for learning” hence it was a possible initiative for service providers to enhance flexibility in their programme offerings to enable in service executives and students with time constraints to participate conveniently in continuing education. In addition to designing courses with flexibility, for the majority of working students, employers’ support for attaining continuing education is of paramount importance. Employers must therefore be encouraged to endorse the further education of its employees as they are essentially equipping themselves with additional skills and knowledge that could potentially enhance their productivity and ability at the work place.

An area of particular focus could be further placed on the continuing education for senior citizens aged 65 or above as well as the more senior spectrum of the labour force. Government had recently issued a consultation paper on extending the retirement age of civil servants along with extended employment for retired persons. There is a trend of both the public and private sectors to extend the employment horizon of working staff in anticipation of a full employment economy. Although those aged above 65 are not covered by the CEF Scheme subsidies, in line with an aging population and longer life expectancy, service providers could consider this to be an opportunity for development. It is evident that in today’s medically advanced society, individuals could still contribute to the workforce beyond their designated retirement age. It is anticipated that by 2020 one in three persons in Hong Kong would be above the age of 50 hence the silver top market represents an opportunity for the continuing education market. Studies on the learning experiences of older adults in Hong Kong purported that elderly people could regain their confidence and strength through continuing education by enhancing their interpersonal communication skills and self-value. Continuing Education service providers could consider the development of programmes targeting at the senior leaners to enable them to rejoin or contribute to the workforce as well as maintain societal focus by achieving true lifelong learning.

**Growing Importance of Sustainable Development**

The importance of sustainability is gaining momentum in terms of public awareness. In essence sustainability refers to the balance of economic, environmental and social considerations in the course of development. Sustainable development is therefore development that meets the needs of the present without compromising the ability of future generations to meet their own needs.

In a fast pace, economically driven and developed society like Hong Kong, the concepts of sustainable development are often sidelined in exchange for immediate present gains and results without due consideration paid to the consequences for future generations. As sustainable development requires a change of mindset to bring about full integration of the needs for economic and social development with that to conserve the environment, there is still a long road ahead for sustainable development in Hong Kong.

Government is playing a vital role of facilitating sustainable development in the domains of environmental protection, waste reduction and recycling. Government has set environmental protection as one of the priorities of the current-term and adopted various measures in the areas of air protection, waste management, green building and historic buildings conservation. In March 2013, the Environment Bureau (ENB) announced a Clean Air Plan for Hong Kong aiming to achieve the new Air Quality Objectives by 2020. Government had reached a consensus with the transport industry to phase out some 82,000 pre Euro IV diesel commercial vehicles while newly registered diesel commercial vehicles will be subject to a service life limit of 15 years with effect from February 2014. The scheme is expected to cost up to HK$11.7 billion for providing ex-gratia payment to registered owners to phase out their vehicles. The Food Wise Hong Kong Campaign aims at reducing food waste is running successfully and gradually changing attitudes towards food wastage via an intense publicity programmes. In 2013, the Council for Sustainable Development established by the Chief Executive to promote sustainability in Hong Kong was in the process of seeking public engagement on municipal solid waste charging. In the area of recycling, the Steering Committee to Promote the Sustainable Development of the Recycling
Industry was established and Government has allocated HK$1 billion to launch a Recycling Fund. These are just some of the many positive sustainable development initiatives taken by Government.

Although the public-sector is rife with sustainable development initiatives, the private sector is comparatively dormant in this domain. Evidently, more companies and organizations view sustainability as a desired goal of development and management but from an operating perspective the concept of sustainable development is still relatively lackluster. Large multi-national companies and conglomerates have adopted sustainability reporting and business practices in line with the international business standard. The Hong Kong Stock Exchange has released a Questionnaire on Environmental, Social and Governance (ESG) Reporting to listed issuers to gather views on sustainability reporting. An ESG Reporting Guide was first appended to Listing Rules in August 2012 and the Exchange plans to raise the obligation level of some recommended disclosures in the Guide to "comply or explain" by 2015. It is anticipated that the ESG reporting will be a requirement for listed issuers in Hong Kong in the near future. Although the framework for disclosure is present, listed companies only represent a small portion of companies in Hong Kong, and many smaller listed issuers may be more interested in fulfilling the compliance requirements rather than to maintain sustainable development initiatives. The Exchange’s mandatory imposition of ESG reporting may raise public awareness of ESG amongst investors and the general public as well as align Hong Kong’s status as an international business community.

Many Small and Medium Enterprises (SMEs) still lack incentives and resources to recognize sustainable development as a pressing business agenda amidst an increasingly costly operating environment. There remains no direct tax or monetary incentives or subsidies for businesses to undertake and engage sustainability initiatives in their daily operations. As SMEs make up 98% of all companies in Hong Kong and employ up to 48% of the workforce, their engagement for sustainable development is still a paramount challenge.

Sustainability initiatives could help SMEs and large corporations manage brand reputation risks arising from supply chain ethics. In the summer of 2014 up to 300 food retailers ranging from large groups to small businesses were exposed for inadvertently using tainted sub-standard “gutter oil” in the production of food products. The tainted oil was from Taiwan that was purchased from seemingly reputable dealers in Hong Kong. Government’s Centre for Food Safety swiftly published a list of all affected retailers. The reputation and business of those on the published list suffered adversely. Reputation risk arising from supply chain ethics can hit even the biggest of companies as proven by the case of McDonalds restaurants in Hong Kong, Macau and China. The world famous fast food giant’s meat supplier Shanghai Husi Food Company was accused of repackaging old meat as new by Mainland authorities. This subsequently led to substantial pullouts of menu items across McDonalds Restaurants in the region and the iconic brand name was tarnished to a grave effect. Supply chain ethics and sustainability is proven to have a substantial and long-lasting effect on businesses of all sizes.

In conclusion, commitment to sustainable development for business is still at an incubation stage in Hong Kong. Businesses in general may have inadequate incentives and access to information about sustainable development initiatives. Government and the business sector should work hand in hand in order to achieve sustainable development for Hong Kong in the long run.

The 2014 Ebola Outbreak

In August 2014, The World Health Organization declared its third ever Public Health Emergency of International Concern in response to the outbreak of Ebola Virus Disease (EVD) in Western Africa. The 2014 Ebola outbreak is one of the largest scale in history. EVD is reaching pandemic status in four West African countries including Guinea, Liberia, Nigeria, and Sierra Leone. EVD is spreading into Central Africa at an alarming rate with confirmed clinical cases in the US and Spain. As of January 3, 2015, a total case count of 20,656 infections; deaths of 8,153; and laboratory confirmed cases of 13,151 of EVD was reported. Experts believe that the actual number of cases and related deaths are materially higher than the reported numbers. There is no licensed treatment or vaccine for Ebola and the death rate for contracted patients is stated to be well above 50%. The World Health Organization (WHO) gave a green light to the use of experimental drugs to combat the disease.
Ebola virus is transmitted from infected animals to humans. It may then spread through human-to-human transmission, with infection resulting from direct contact through broken skin or mucous membranes with the blood, secretions, organs or other body fluids of infected people, and indirect contact with environments contaminated with such fluids. The U.N. health agency has warned that the Ebola epidemic could infect over 20,000 people and spread to more countries. As a response, WHO announced a US$490 million strategic plan to contain the epidemic over the next nine months including the provision of medical supplies, drug treatments and protective clothing for frontline healthcare workers.

As EVD has a relatively long incubation period from 2-20 days with no specific prevention vaccine, it is plausible that Hong Kong as an international transportation hub would receive infected persons in transit or as visitors. A travel health advice to affected regions was issued by Government on 30 July 2014. In response to the threat of EVD, Government’s Centre for Health Protection (CHP) further issued the Preparedness and Response Plan for Ebola virus disease on 20 August 2014. The aim of the plan was to ensure that the medical staff and general population was equipped with the core capacities to prevent, detect, characterize and respond quickly, efficiently and in a coordinated manner to the EVD threats in order to reduce mortality and morbidity. In the plan, detailed practice notes are given to certain high risk industry practitioners such as medical and tourism professionals on precautionary measures and the public were reminded to avoid unnecessary travel to affected areas, maintain good personal hygiene, and be diligent of signs of infection. As of 15 October 2014, there were fortunately no reported cases of EVD in Hong Kong.

Having encountered the SARS epidemic of 2003, Government is taking a proactive stance against EVD before the onset of local clinical cases. The implications of SARS took a heavy toll on Hong Kong’s economy and EVD could potentially cause the same resonance in the local business community. Although the epicenter of contagion for EVD is not local, businesses especially those relying on resources and commodities produced in Africa may face supply and price pressures. Some foreign investments in the affected parts of Africa, including big mining firms have evacuated foreign staff and shut down non-essential operations. This may have an knock on effect on commodities prices and investors has already begun to anticipate the economic impact of the breakout as share prices for companies with a heavy exposure in West Africa have plunged since the epidemic began. Exporters and importers of goods to and from Africa are similarly effected such as timber and rubber products. In terms of both the local and world economy, the economic and health extent of the damage will depend on how far the disease spreads and how long the outbreak lasts.

3. POLITICAL FACTORS

Political Instability Arising From Constitutional Development

Constitutional Development and electoral reform was a contemporaneous issue for Hong Kong society in 2014. The year marks a turning point in the political landscape of Hong Kong. In December 2013, Government published the “Consultation Document on the Methods for Selecting the Chief Executive in 2017 and for Forming the Legislative Council in 2016” to formally commence a five-month public consultation exercise. Amidst dire criticism of the proposed electoral reforms, the State Council of China issued a “White Paper” on 10 June 2014 on “The Practice of the One Country, Two Systems Policy in the Hong Kong Special Administrative Region”. The “White Paper” stressed the Central government’s comprehensive jurisdiction over Hong Kong, and sparked criticism among pan-democratic political parties. The “White Paper” caused high political volatility, as citizens worry that China would further encroach the civil liberties, free press and independent judiciary of Hong Kong.

The pro-democracy movement Occupy Central with Love and Peace (OCLP) had advocated actions of civil disobedience in the form of an operation to occupy Hong Kong’s financial district to lobby for “real” democratic process in Hong Kong. OCLP conducted an unofficial civil referendum online in which nearly 800,000 people purportedly voted at the end of June 2014. The majority of voters requested that Hong Kong’s 7.2 million residents be allowed to choose their own leader. Concurrently the pro-Beijing group Silent Majority conducted a signature campaign in which allegedly 1.5 million people signed to oppose any actions of civil disobedience and
occupying Central. Opposition to the Occupy Central movement stated that such an operation would paralyze the financial district as well as adversely effecting the global image of Hong Kong.\(^{285}\)

As the debate on constitutional development progressed, the society was exposed to increasing polarity of opinion surrounding the political issues at hand. This strong divide of opinion in society arising from the constitutional debate has also led to other problems such as Legislative Council meetings becoming grounds for deadlock through frivolous questioning and stalling by pan-democratic members as well as a noticeable increase in violence during the meetings.\(^ {286}\) On 1 July 2014 protestors\(^ {287}\) took to the streets of Hong Kong\(^ {288}\), the turnout was the largest number in the past few years.

On 31 August 2014, the Standing Committee of the National People's Congress (NPCSC) announced its decision on proposed electoral reform.\(^ {289}\) The decision imposes the standard that "the Chief Executive shall be a person who loves the country and loves Hong Kong," and requires "the method for selecting the Chief Executive by universal suffrage must provide corresponding institutional safeguards for this purpose." The decision states that for the 2017 Chief Executive election, a nominating committee, similar to the present Election Committee system, be formed to nominate two to three candidates, each of who must receive the support of more than half of the members of the nominating committee. After popular election of one of the nominated candidates, the Chief Executive-elect "will have to be appointed by the Central People's Government." The process of forming the 2016 Legislative Council would be unchanged, but following the new process for the election of the Chief Executive, a new system to elect the Legislative Council via universal suffrage would be developed with the approval of Beijing.

With the NPCSC decision seemingly finalized, a dramatic turn of events occurred. Towards the end of September, the constitutional development debate quickly became an unprecedented civil disobedience movement in the history of Hong Kong. On 26 and 27 September 2014, student groups Hong Kong Federation of Students and Scholarism mobilized students to boycott classes.\(^ {290}\) This was followed by the unexpected announcement by OCLP organizers that the Occupy Central civic disobedience movement would immediately commence at the early hours of 28 September 2014.\(^ {291}\)

The events that followed could be summarized as the most extreme political action in Hong Kong since the handover and perhaps the inception of the former colony. In an attempt to disperse the crowd of an estimated number of 30,000 protesters\(^ {292}\) that piled into Central and Admiralty to join the student protesters, police used tear gas.\(^ {293}\) The resulting resonance of the action led to widespread support of the Occupy Central from members of the general public. For the month that followed, occupiers not only successfully occupied Central but also vital areas including Admiralty, Causeway Bay, as well as Mong Kok resulting in widespread traffic paralysis.\(^ {294}\)

The Occupy Central movement came to an end on 15 December 2014. The more important issue of a divided society calls for concern with the functions of Government being affected by the announcement of an “Uncooperative Campaign” by pan democratic legislators\(^ {295}\), which would worsen the Executive-Legislative discord. On the onset of the constitutional development debate causing a rift in the Legislative Council, this may indicate an adverse effect on the efficiency and competitiveness of Hong Kong.

**China in Global Political Dynamics**

China was the world’s second largest economy in 2013 in terms of GDP.\(^ {296}\) It is anticipated that it will overtake the US by 2030, and become the world’s largest economy.\(^ {297}\) Combined with the Mainland’s formidable military strength, which is ranked third amongst the world economies after US and Russia\(^ {298}\), China will inevitably exercise increased influence over the landscape of global politics in the near future.

The US announced its return to Asia policy in 2011\(^ {299}\) to protect and enhance America’s long-term political, economic and security interests.\(^ {300}\) The resulting effect has led to more US military personnel stationed in the Asian Pacific region than at any other time since World War II.\(^ {301}\) Commentators stated that the prolific military maneuvers in the region are conducted to send a message to China on US’s military presence as well as co-operation with its regional partners to
keep China in check.\textsuperscript{302} The US also increased its exportation of weapons to the region, delivering 23\% more advanced warplanes and warships to Asian countries in 2013.\textsuperscript{303} The US involvement in the region posts concern for China with policies aimed to restrain the Mainland’s dominance in the region.

China unilaterally announced the introduction of the East China Sea Air Defense Identification Zone (ADIZ) in November 2013 without any consultation with regional neighbors.\textsuperscript{304} China’s ADIZ covers infringed airspace from Japan, Taiwan, South Korean and Philippines.\textsuperscript{305} Effected countries and the US declared the new ADIZ to be illegitimate. This issue has caused tension in the region.

Under the context of US involvement and tense political relations in the region, Sino-Japanese relations developed into diplomatic deadlock in 2014. Sovereignty claims over the Diaoyu Islands were demonstrated by clashes in the waters and the use of drone aircraft\textsuperscript{306} raised fears that the conflict could trigger escalated hostilities.\textsuperscript{307} Japanese Prime Minister Shinzo Abe’s nationalist stance has attracted concerns and disapproval from China. Abe’s visit of the Yasukuni Shrine in December 2013 and the reinterpretation of Article 9 of the Japanese Constitution in July 2014 to allow Japan’s Self-Defense forces to defend other allies in case of war posed pressures on both sides. The animosity and tense Sino Japanese relations are likely to continue in the near future.

Border disputes continue to cause pressures on regional diplomatic relations. China imposed a fishing permit rule in the South China Sea amidst strong protest from the Philippines. In March 2014, Philippines filed a case to an international arbitration tribunal in The Hague against China’s South China Sea claims.\textsuperscript{308} Anti-Chinese sentiments are building in the Philippines with the occurrence of anti-Chinese protests becoming more regular.\textsuperscript{309} Comparable circumstances in Vietnam were caused by disputes involving oil exploration rights at the South China Sea.\textsuperscript{310} Violent anti-Chinese protests erupted and Chinese owned factories became attack targets. Chinese businesses evacuated staff and ceased operations and were adversely effected as a result of the conflicts in Vietnam.

China’s foreign policy and relations with neighbours supplemented by US military presence continue to contribute to the instability of the Asian Pacific region. As Renminbi appreciates and the costs of production in China continues to rise, some manufacturing businesses have already established their production facilities in South East Asia or are considering to do so in the long run.\textsuperscript{311} The increasing negative sentiment towards Chinese persons and businesses are evident in neighbouring countries and may effect business operations as demonstrated by the Vietnam demonstrations. Continual political instability of the region could also take its toll on regional financial markets and economies as investor and consumer confidences are effected.
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