Why Now is the Best Time for Hong Kong's Economic Transformation

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In my article published in this column in April, I pointed out the "positive non-interventionism" policy impacting Hong Kong for over half a century had indirectly led to industrial homogeneity and social immobility. I believe it is high time to change and come up with viable solutions to create diversified industries and jobs. Focusing on three key areas listed below, this article will attempt to analyse why the next few years will provide the golden opportunity for economic transformation in Hong Kong.

Successive versions of industrialization

First of all, the way I see it, now is the time for economic transformation driven by interaction among industries, universities, and research institutes as well as high-end industries to succeed.

Since former Chief Executive Mr Leung Chun-ying called for the reindustrialization of Hong Kong for the first time in his Policy Address in 2016, the Government of the Special Administrative Region (SAR) has, through such institutions as the Innovation and Technology Bureau, Science Park, and the Hong Kong Productivity Council, provided direct subsidy, technical support, and rental concessions to steer thousands of reindustrialization projects. The industry sector nevertheless contributes to less than 1% of Hong Kong's Gross Domestic Product (GDP). Compared with the other three Asian Dragons — Singapore, South Korea, and Taiwan, boasting a GDP share at over 20%, there is still much room for development and improved progress for Hong Kong's reindustrialization.

The information technology-driven Third Industrialization during the period from the 1970s to 1980s made it easier for every part of the production chain to be subcontracted to foreign suppliers, enhancing the efficiency of the international division of labour. Due to the rapid opening up of the Chinese economy before the 1990s, significantly-raised productivity during the decades-long economic reform,

and a huge labour population released from the rural areas, Hong Kong manufacturers have taken the opportunity to relocate most of their production lines to the Pearl River Delta (PRD). At their peak, these manufacturing enterprises employed more than three million workers in the PRD, establishing the so-called "shop in the front, factory in the back" production model while hollowing out Hong Kong's industries.

All that said, if effective use can be made of the Fourth Industrialization (Industry 4.0), which has been led by the Internet of Things (IoT) over the past few years, it will be possible for Hong Kong to realize reindustrialization.

By utilizing technologies including artificial intelligence, big data, and 3D printing, manufacturers can explore opportunities for flexible servitization of products, enhance productivity, lower production and storage costs, and overcome hurdles to developing high-tech industries resulting from exorbitant rent and wage costs over the years. Relying on "Industry 4.0" technology running through the production processes involving supply chain partners, small and medium enterprises (SMEs) can participate in more sophisticated division of labour worldwide.

For instance, Hong Kong manufacturers can consider making use of smart production technology to create high-value-added products locally researched and developed, e.g. orthokeratology lenses, smart watches, medical equipment and supplies, etc. The goal is to go high quality in view of the expanding middle-class markets in the Mainland and across Asia. Should the need for increased production output arise, IoT technology can also play a role in connecting with other production bases in the region to satisfy market demand by flexibly increasing supply.

Hong Kong's edge in the region lies in its wealth of basic-research manpower and experience, a relatively solid intellectual property rights regime, and world-class sea and air freight facilities.

By leveraging the edge in these areas, Hong Kong manufacturers can take part in upstream and downstream activities along the global value chain — research and development (R&D) of high-end products and the final assembly of precision parts respectively. Export to countries around the world will be greatly facilitated by using IoT technology in smart manufacturing.

Further to backing Hong Kong to capitalize on its existing advantages in such areas as finance, shipping, and trade in the region and highlighting the SAR's need and ability

to reindustrialize in the Guangdong-Hong Kong-Macao Greater Bay Area (GBA) Development Plan released in 2019, the Central Government makes known in the 14th Five-Year Plan its support for Hong Kong's development of an international innovation and technology (I&T) hub.

Given the I&T synergy between the national policy and the Industry 4.0 revolution, I feel optimistic about Hong Kong's economic transformation.

The new world order

As the China-US struggle is set to continue in the foreseeable future, the geopolitical situation is nothing but uncertainties. Moreover, the governments of various countries will introduce policies to reinforce the resilience of the supply of necessities and key components in the post-COVID-19 era. In the realm of sensitive technologies, e.g. 5G, different regions will probably come up with their own different standards. Given the new normal worldwide, it will be essential for enterprises to be prepared for the impact from natural disaster or worsening international relations lying ahead. Hence the focus will be on spreading out manufacturing sites, reducing a cluster of production facilities in the same region to minimize production cost. As a result, international trade will become regionalized and fragmented, offsetting the previous gains from economy of scale. On the contrary, this will open up opportunities for SMEs to participate in the global supply chain while Hong Kong manufacturers are also likely to benefit from this reconstruction process of the trade chain.

As for the many Chinese scientists and technological research professionals working in the US, faced with increasingly unfair treatment as a result of biased law enforcement against Chinese people, they may consider relocating to Asia. It would be sensible for the SAR Government to raise incentives by launching a talent recruitment programme to attract this group of talent to come and work in Hong Kong, contributing to the scientific research and economic transformation in Hong Kong and the region. In the 2021–22 Financial Budget, the Government announces that it will earmark funding for local universities to recruit I&T talent from abroad. Adjacent to the Hong Kong Science Park, the InnoCell will soon provide affordable living and collaborative spaces complete with smart-technology facilities for the I&T community. This is an encouraging start. Further support may be rendered if the facility proves to be a success.

In addition, to prepare for the challenges of the new era, the Central Government puts particular emphasis on the "dual circulation" economic strategy in the 14th Five-Year Plan released this year. In terms of the internal circulation, the policy will boost domestic demand and preserve the integrity of the production chain. As for the external circulation, the aim is to consolidate China's commercial ties with other countries in Asia. The Regional Comprehensive Economic Partnership (RCEP) signed by 15 Asia-Pacific countries in November 2021, in particular, as the world's largest free-trade pact, is expected to create in the region a middle-class consumer market with a population of one billion within the next decade. The dual circulation strategy is set to bring tremendous opportunities to local companies and professionals which are fully prepared. As Hong Kong's trade landscape is bound to undergo a big change, the authorities concerned should help companies to transform effectively and enter the emerging markets.

New economic-policy vision

I recently reread the book *Made by Hong Kong* published in 1997. The eight co-authors of the book are academics in fields ranging from politics to nuclear engineering from my alma mater, Massachusetts Institute of Technology (MIT). Invited by Hong Kong's business community, they wrote their analysis and made their recommendations after interviewing 350 business people and institutions from 1995 to 1996. Andrew Bernard, an economist I have known for years, told me in person that for this research project, he made 20 visits to Hong Kong from Boston within the two years.

The study covers six industries, namely biotechnology, electronics, information technology, clothing and textiles, capital markets, and other manufacturing industries. The eight academics are convinced that it is imperative for Hong Kong to elevate its industrial development, formulating a high-tech, knowledge-based roadmap for industries as the way forward. They make the following six recommendations accordingly.

1) The Hong Kong economy must bolster its innovation capabilities in product and production process. In addition to close collaboration between industry and universities, efforts should be made to build corporate brand image. Both the

Government and the industrial sector must substantially raise the level of investment in R&D, especially in applied research.

2) To improve the local labour workforce, the higher-education sector should focus on nurturing talent in applied-science, product R & D, and design. It is also vital to enhance the English proficiency of secondary and primary students.

3) Public institutions charged with protecting intellectual property rights should be expanded and local and foreign companies in Hong Kong should be encouraged to engage in scientific research and innovation.

4) To promote new-technology-based enterprises while the Science Park, still in the pipeline at the time, is strongly recommended to create a decentralized "virtual" network for start-ups and technological development of enterprises in the early stages.

5) To enable more technical personnel to join the Government. A revolving-door mechanism should be in place to recruit industry experts and academics to take up provisional but full-time executive portfolios set up by the Government.

6) To attract more skilled workers from the Mainland and overseas through refined immigration policy, housing subsidies, and subsistence allowances for people coming to work in Hong Kong from abroad.

The above recommendations from 24 years ago not only still apply in the local scene today but are also urgently required. Regrettably, Hong Kong's economic transformation envisaged by the MIT team has not materialized because having undergone its first economic transformation in the 1950s, despite the twists and turns through the years, Hong Kong has still been able to gain from various global political and economic changes. First, when the Chinese economy was not yet fully open before 1978, there were economic gains from Hong Kong's role as the bridge between China and the West. Then, as China gradually opened up to the world, there were economic gains for Hong Kong as the intermediary, including those from foreign investors entering the Mainland market through Hong Kong in early 1990s. Other gains for the SAR came from China's accession to the World Trade Organization in 2001 and from Mainland capital "going out" via Hong Kong over the past decade.

It was an eventful era, coupled with the general fear of policy revisions in the local community as discussed in Professor Lui Tai-lok's book, *An Embarrassment: Hong*

Kong Has Yet to Find Its Way into the "One Country, Two Systems" Agenda (尷尬：香港社會還未進入一國兩制的議題). Any proposal to introduce sweeping economic-policy changes will fall beyond the comfort zone of the "non-intervention" principle governing the economic lifeline under the British colonial rule. Nevertheless, as Hong Kong is faced with deep-seated structural problems surfacing over the past two decades, e.g. supply and demand imbalances in land and housing and industrial homogeneity, different sectors of the community such as financial executives have openly acknowledged that non-interventionism characterized by the catchphrase "small government, big market" is already outdated. Therefore, I have high hopes for Hong Kong's third economic transformation.

The recent 20-year speedy development of the Chinese economy is probably something not even the insightful co-authors of *Made by Hong Kong* could have imagined back in 1997. But as times have changed, the SAR's economic policy at present has to align itself with China's overall economic plan. Above all, it has to synergize and supplement the economic development of the GBA to seal a win-win situation.

However, given the basic principles mentioned above, while the eight MIT professors' recommendations — for the most part — may not have been adopted by the SAR's policymakers, they still bear landmark significance to inspire the blueprint design for Hong Kong's economic transformation.