SCMP.COM

South China Morning Post

China Economy

Are Hong Kong’s protests crushing the city’s role in China’s Greater Bay Area plan?

Greater flow of people, capital and goods across southern China would improve competition and bolster growth as trade war continues to bite

To narrow gap with Hong Kong, Beijing has introduced preferential policies for taxation and foreign investment this year

Topic | China economy

Karen Yeung

Published: 8:30pm, 20 Aug, 2019

Joshua Rotbart, a gold trader and shipper, has been watching Hong Kong's unfolding political crisis with keen interest, fearing that further protests could damage the city's leading position in the gold market.

Before this past weekend's peaceful demonstrations, confrontations between the police and protesters had become increasingly violent over the summer, culminating at Hong Kong International Airport last week when hundreds of flights were cancelled.

The cancellations disrupted the transport of gold arrivals into the city, including those in transit to mainland China, raising the question of whether Beijing would look for other avenues to accumulate its holdings. More importantly, the protests have fuelled worries of whether Hong Kong's role as a global financial centre in China's Greater Bay Area plan will shrink.

"Hong Kong is the gateway to gold for China," said Rotbart, founder of J. Rotbart & Co, a firm that trades, ships and stores physical gold and other precious metals. "But a lot of gold is being exported directly to China and our feeling is that the Chinese government is looking for other avenues. They don't want everything to come via Hong Kong any more."

Hong Kong's biggest gold-storage facility is on the ground floor of a building within the airport. Rotbart estimated that at least HK$2 billion (US$294 million) worth of the precious metal had fled the city in the past week or so.

He said only time would tell to what extent Hong Kong's leading gold market would be affected. In the meantime, competition is building, and could come from its closest neighbour – Shenzhen, which borders the city and is one of nine urban centres in the southern province of Guangdong, along with Hong Kong and Macau, that are part of the Greater Bay Area development plan.

On Sunday, the State Council, China's cabinet, issued a directive cementing Shenzhen's key role in science and technology in the plan, granting it special policy leeway, including a leading role in the internationalisation of the Chinese yuan.

The directive expands on the national Greater Bay Area blueprint released in February that confirmed Hong Kong (international finance centre and airport hub), Macau (leisure centre), Shenzhen (innovation centre) and Guangzhou (transport and training hub) as the four engines to drive the area's development. It will be underpinned by the "one country, two systems" principle for the two special administrative regions (SARs) of Hong Kong and Macau.

> **Hong Kong will have to demonstrate to Beijing that its standards and norms help the Greater Bay Area become an economic powerhouse in the shortest period of time**
> **Robert Grieves**

Under the initiative to boost the yuan internationalisation process, Hong Kong is linking up with Shenzhen's gold market, allowing mainland investors to trade yuan-denominated gold in the city and receive the physical gold bars in the Chinese city's Qianhai area.

Traditionally, gold is transported on commercial flights from Switzerland and is parked in Hong Kong before being delivered by banks to China based on a quota system.

But Hong Kong's primacy as the region's top financial centre has been thrown into question by the protests.

"Hong Kong will have to demonstrate to Beijing that its standards and norms help the Greater Bay Area become an economic powerhouse in the shortest period of time," said Robert Grieves, chairman of the American Chamber of Commerce in Hong Kong.

Fortunately for Hong Kong, its SAR status sets it apart from the nine Chinese cities that are restricted by Beijing's draconian capital controls. Those controls put a lid on flow of funds and domestic markets, and are still significant barriers between the mainland and the rest of the world, according to John Lam, analyst at UBS Securities Asia.

"Hong Kong uses US dollars and Hong Kong dollars, which are freely convertible. So if foreign companies wanted to transact in US dollars, it would be much easier to do this in Hong Kong as the mainland faces strict capital controls," Lam said.

The domestic Chinese equity and bond markets are only partially opened to foreign investors via approved investment schemes such as the Stock and Bond Connect programmes.

In contrast, the markets in Hong Kong, which has a free-market economy, is one of the world's most robust capital-raising platforms and has helped mainland Chinese companies raise funds since Beijing began introducing economic reforms 40 years ago.

Nonetheless, analysts said, the Hong Kong protests, were a wake-up call for Beijing to accelerate the opening up of the Greater Bay Area, Beijing's vision for an integrated powerhouse that is the cornerstone of Chinese President Xi Jinping's strategy to win the battle for global technology and economic supremacy. Weeks of demonstrations have underscored Hongkongers' deep-seated apprehension that integration with the mainland is a double-edged sword – one that brings economic returns, but also erodes the city's governance standards, as well as business and regulatory environments.

"Because of Hong Kong's protests, and along with the trade war with the US, there is a acknowledgement that Shenzhen and Shanghai need to accelerate their market liberalisation," said Ding Wenjie, economist at CMB International Securities.

Three months of increasingly violent clashes between extradition protesters and the Hong Kong police are leaving residents uncertain about their home city.

Because of Hong Kong's protests, and along with the trade war with the US, there is a acknowledgement that Shenzhen and Shanghai need to accelerate their market liberalisation

Ding Wenjie

Such sentiments, said Terence Chong, professor from the department of economics at the Chinese University of Hong Kong, could prompt some Hong Kong residents to now view Greater Bay Area cities as "quieter and safer", which would accelerate integration of the city with the mainland.

"The reason why some [Hong Kong] people were unwilling to move to the mainland before was because they thought the living standards and the political freedom there were lower," Chong said.

"But given the current situation, they may now think that Hong Kong is unsafe and that its conditions are actually worse off than the mainland's."

Leo Yang, partner at the tax division of Deloitte, said Beijing this year launched preferential policies for individual income tax and foreign direct investment in the mainland portion of the Greater Bay Area to narrow the gap with Hong Kong, which had the advantage of a far lower and simpler tax rate system.

While the bay area development plan had challenges, there were genuine synergies between the economies of the cities, which investors and businesses had been leveraging for decades, said Sharmila Whelan, deputy chief economist at Aletheia Capital.

Mainland Chinese companies had established 12,642 regional headquarters or local offices in Hong Kong in 2017, up from 725 a decade ago, she said.

The number of approved Hong Kong-invested companies in Guangzhou reached 20,155 last year and contracted direct investment from Hong Kong totalled US$95 billion. Now, more than 1,100 mainland companies with a combined market value of over US$2 trillion are listed in Hong Kong, accounting for over 60 per cent of the market's total capitalisation.

Source URL: https://scmp.com/economy/china-economy/article/3023615/are-hong-kongs-protests-crushing-citys-role-chinas-greater