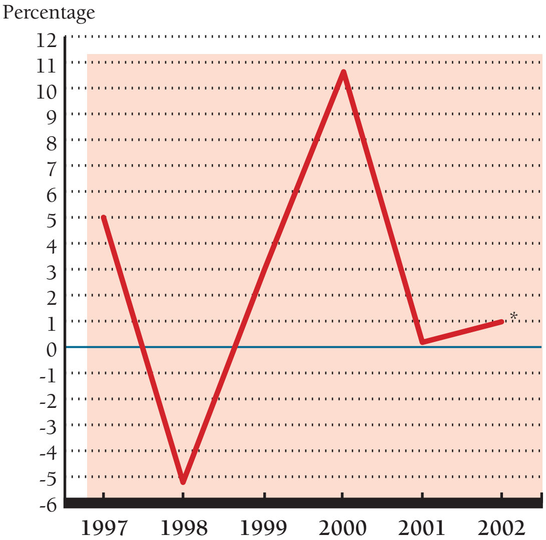
The Economy

Economic performance

GDP Growth 1997 - 2002



**Forecast*

If one issue has occupied the minds of Hong Kong people over the past five years it has been the state of the economy.

The Asian financial crisis buffeted Hong Kong from late 1997 until the end of 1999. A robust but short-lived recovery in 2000 gave way to insignificant growth in 2001 on the back of the global economic slowdown.

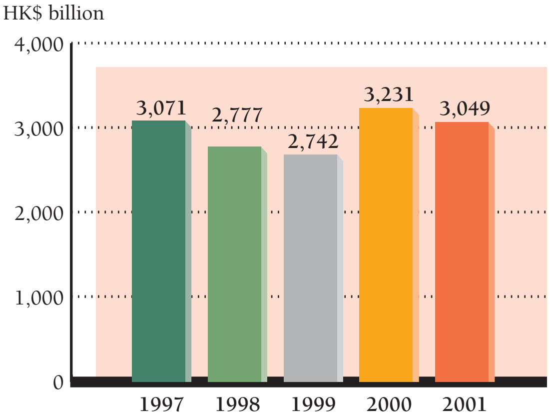
Per capita GDP stood at HK$187,700 (US$24,100) in 2001, but is still considerably lower than the 1997 levels of HK$204,007 (US$26,400).

Since 1997, annual trade flows have averaged HK$2,974 billion, about 3% lower than 1997 total trade of HK$3,071 billion. The year-on-year value of total trade dropped in 1998 and 1999 before rebounding sharply in 2000 and dropping again in 2001. Total trade by value dropped by HK$56 billion, or 8% year-on-year, in the first quarter of 2002.

Since late 1997, Hong Kong's economy has been grappling with a painful restructuring that has seen asset prices drop considerably and unemployment rise to a record level of over 7%.

The bursting of a property and stock market bubble in late 1997 and early 1998 has had a major and prolonged impact on consumer sentiment. Prices (measured by the Composite Consumer Price Index) have dropped for more than three years and are forecast to drop a further 2.8% for 2002 as a whole. This is due, in part, to the combined effects of government relief measures to help lower costs in the economy.

Total Trade 1997 - 2001



In general, lower housing and office rentals have helped boost Hong Kong's competitiveness. Housing prices have dropped by more than 50% off their mid-1997 peaks, while rentals have eased 30%.

Hong Kong's currency, linked since 1983 to the US Dollar at a rate of HK$7.80 = US$1, has remained rock solid over the past five years. In line with US interest rates, local interest rates came down considerably during 2001.

In August 1998, the currency came under speculative attack by some aggressive market players. The government took the unprecedented step of launching a defensive incursion into the stock and futures markets to restore a level playing field.

During a one-month operation, the government spent a total of HK$118 billion (US$15 billion) buying the 33 constituent stocks of the Hang Seng Index. The stocks bought during that exercise have gradually been put back onto the market in an orderly manner through a Tracker Fund, launched in November 1999, that tracks the movement of the Hang Seng Index.

Financial sector

The financial sector has undergone major reform and enhancement over the past five years to boost the attractiveness of Hong Kong as an international financial centre.

Following the 1998 speculative attacks on the currency, the Hong Kong Monetary Authority boosted the transparency of the Currency Board System to help prevent further manipulation and to provide a more complete picture of the strengths of the reserves underpinning Hong Kong's currency.

Reforms were also introduced to further enhance competitiveness, efficiency and innovation in the banking sector which led to the elimination of all interest rates rules.

To strengthen Hong Kong's competitiveness as an international financial centre, the Financial Secretary in 1999 announced a three-pronged reform of the securities and futures market.

Key elements of the reforms have been to:

- Upgrade market infrastructure by putting in place state-of-the-art trading, clearing and settlement facilities capable of further integration with the rest of the financial markets
- Modernise market structure by demutualising and merging the Exchanges and their associated Clearing Houses and separating ownership from trading rights. The securities and futures exchanges and clearing houses were merged and listed on the Stock Exchange of Hong Kong in June 2000.
- Consolidate the 10 Ordinances governing the securities and futures market and modernise the regulatory framework for maintaining a fair, orderly and transparent market on par with international standards and practices. The Securities and Futures Ordinance, passed by the Legislative Council in March 2002, will help to further consolidate Hong Kong's position as a major international financial centre and the premier capital formation centre for the Mainland of China.

A NASDAQ-style second board, the Growth Enterprise Market (GEM) was launched in November 1999. The GEM provides a channel for emerging and growing companies, many in the technology field, to raise capital. At the end of April 2002, more than 125 companies with a market capitalisation of almost HK$70 billion (US$9 billion) were listed on the GEM.

In late 2000, a pilot programme was launched to allow the 'live trading' in the Asian time zone of seven leading NASDAQ stocks, six of which are technology or biotechnology counters.

A US Dollar real-time-gross-settlement (RTGS) payment system has been well received by the financial community since it was launched in August 2000. There are currently 64 direct and 125 indirect participants. Among the indirect participants, 84 are from overseas.

Turnover has grown steadily from 2 700 to 3 000 transactions worth over US$4 billion in 2001 to more than 3 000 transactions with a value of US$4.9 billion by January 2002. Payment Vs Payment transactions accounted for about one third of US Dollar RTGS turnover value in 2001.

Derivatives warrants were reintroduced into the market in January 2002 and quickly re-established demand, accounting for more than 5% of daily turnover.

To meet rising competition, a Task Force on Financial Market Development led by the Secretary for Financial Services was set up in 2002 to explore ways to increase market liquidity by encouraging new players and developing new products and services.

Mandatory Provident Fund System

The Mandatory Provident Fund (MPF) System was introduced in December 2000 to help Hong Kong workers save financially for their futures.

This privately-managed, compulsory retirement protection scheme has added greater depth to Hong Kong's financial services sector and has had a positive affect on the long-term development of the bond and securities markets.

Under the system, all employees aged between 18 and 65 (unless exempt) contribute 5% of their monthly wage, up to a maximum of HK$1,000 (US$128). Their contribution is matched by the employer. Self-employed people also contribute 5% of their income to the scheme, subject to the same maximum.

At the end of its first year of operation, accrued assets of MPF schemes had surged to HK$36 billion (US$4.6 billion). By the end of April 2002, 92% of employers, 96% of relevant employees and 85% of self-employed persons had enrolled in MPF schemes.

MPF schemes are expected to inject up to HK$60 billion (US$7.7 billion) annually into the fund management market by 2030.

2002-2003 Budget

The 2002-2003 Budget at a glance*

Total public expenditure	HK$287.18 billion *(US$36.82 billion)*
Government expenditure	HK$259.8 billion *(US$33.31 billion)*
Government revenue	HK$214.6 billion *(US$27.51 billion)*
Consolidated deficit	HK$45.2 billion *(US$5.79 billion)*
Fiscal reserves *(at 31-3-2003)*	HK$325.6 billion *(US$41.74 billion)*

**Forecast*

In his first Budget since taking office in May 2001, the Financial Secretary, Mr Antony Leung, outlined his vision for Hong Kong's economic development and proposed measures to restore fiscal balance by 2006-07 and reduce the share of public expenditure in the economy. A package of one-off relief measures to help the community was also announced.

The Financial Secretary revealed in his Budget of March 6, 2002, that Hong Kong's economy grew by 0.1% in real terms in 2001, and was forecast to grow by 1% in 2002. A trend growth rate of 3% in real terms was predicted in the medium-term (from 2002 to 2006).

Consumer prices fell by 1.6% in 2001 and were forecast to decline by 2.8% in 2002. Unemployment for 2001 as a whole was 5.1% but had since risen to a record high of over 7% in early 2002.

Mr Leung said Hong Kong had to capitalise on its strengths and needed to focus on high-added-value economic activities to move up the value chain. He believed there were four economic sectors in particular that could foster further economic development and create jobs – financial services, logistics, tourism, and producer and professional services.

He said the government would upgrade the quality of manpower and increase the number of talented individuals, by improving education and attracting outside talent. It would also enhance flows of people, goods, capital, information and services to and from the Mainland.

Mr Leung forecast a Budget deficit of HK$65.6 billion (US$8.4 billion) for 2001-2002 compared to the original estimate of HK$3 billion (US$385 million). A deficit of HK$45.2 billion (US$5.8 billion) was forecast for 2002-03 from revenues of HK$214.6 billion (US$27.5 billion) and expenditure of HK$259.8 billion (US$33.3 billion).

But he made a firm commitment to restore fiscal balance by 2006-07. From 2003-04 onwards, government spending would only be allowed to grow by 1.5% in real terms per year over the medium-term, half of the trend economic growth rate of 3%.

He pledged to reduce public expenditure as a percentage of GDP and set a target of bringing it down from its current level of 23% to 20% of GDP or below by 2006-07.

Because of difficult economic conditions, no major changes were introduced on the revenue side. However, Mr Leung signaled that the government would have to consider other options to raise revenue or reduce expenditure other than those outlined in the Budget if the fiscal situation did not improve in the medium-term.

Mr Leung also unveiled a HK$6.4 billion (US$820 million) relief package to help Hong Kong citizens and businesses ride out the economic downturn.

The concessions would mean that about 85% of ratepayers (about 2.3 million) would pay no rates for one year, 80% of households and businesses would pay no water and sewage charges for one year, and over 600 000 businesses would be exempt from paying business registration fees for one year.

China's entry to the World Trade Organisation

Hong Kong's strong links with the Mainland

- Hong Kong is the most important entrepot for China, handling about 30% of the Mainland's foreign trade
- Hong Kong is the largest external investor in the Mainland, accounting for about half – or US$187 billion – of all realised direct investment in China by end-2001
- Hong Kong is the largest, single external investor in all Mainland provinces. There are about 110 000 Hong Kong firms investing in the Mainland
- About five million people are employed in neighbouring Guangdong Province by more than 36 000 companies wholly or partly-owned by Hong Kong enterprises
- More than 190 000 Hong Kong people work in the Mainland, accounting for 6% of the employed population in Hong Kong. About 80% of them work as managers, professionals or administrators

China's entry into the World Trade Organisation (WTO) in December 2001 has changed the face of the global economy. It has thrown open a huge market of 1.3 billion people and injects greater transparency and certainty into a vast and growing trading regime.

As the Mainland's closest trading and investment partner, Hong Kong stands to be a key beneficiary of this development.

Hong Kong enterprises will face increased competition from international companies vying for business in the huge Mainland market. But at the same time, market potential will continue to expand – trade flows in the Mainland are projected to increase quickly and significantly from their current annual level of US$510 billion. Their depth of knowledge and experience in the Mainland will give them an unrivalled edge in seizing opportunities.

China's WTO accession will not be a zero-sum game for Hong Kong – China's market is too big for just one or two major cities to take the lion's share of trade and investment opportunities. The sheer size and diversity of the market presents much room for further co-operation and partnership. In the process, Hong Kong and Mainland cities can make best use of their comparative strengths and advantages, creating a 'win-win' situation.

For example, in Guangdong and adjoining provinces there are more than 270 million people. On the eastern seaboard, there are now some 230 million people in the provinces around Shanghai and the Yangtze River Delta. Further north Tianjin is well-positioned in a market now of over 160 million people. Looking west Chengdu and Chongqing have the potential to service another 250 million people, of which almost 85 million live in Sichuan province.

While co-operation in services will remain the key theme in the prosperous coastal regions and big cities like Guangzhou, Beijing and Shanghai many other opportunities in the Mainland's domestic market will come from the developing, resource-rich inner and western provinces.

The Chief Secretary for Administration, Mr Donald Tsang, led a 280-strong Hong Kong delegation to Western China in May 2001 to assess business opportunities, promote Hong Kong's strengths and advantages and better understand the potential for development of western China's resources. That landmark visit has paved the way for further activities to help cement closer economic links between Hong Kong and western cities, where the Mainland government is intent on developing the next high-growth areas.

Hong Kong businesses will have to work hard to leverage their existing strengths and contacts in the Mainland to capitalise on the enormous opportunities that will emerge in China over the next few decades.

Hong Kong's existing business links – as well cultural and language bonds – can also be an enormous resource for overseas companies, especially small and medium-sized enterprises, wishing to do business in China.

By joining forces with established Hong Kong businesses, overseas companies will be able to bring their products and services to the Mainland market as well as draw on the decades of experience of Hong Kong's entrepreneurs. Hong Kong companies have already joined forces with joint venture partners in the Mainland to do just that.

Shanghai

Hong Kong's quality of life – boosted by good education and health services ... – will help to ensure that it remains China's first entrepot for several years to come. But the pace of change in Shanghai, and the excitement the city generates among foreign investors, could quickly narrow the gap. If Hong Kong is to remain superior to both Shanghai and Shenzhen, it will have to reinforce both its strengths: its legal independence, and its economic interdependence.
– The Economist, March 29, 2002

Shanghai's impressive development over the past decade has led some to question whether Hong Kong can retain its role as the premier international financial centre for China.

Often, comparisons between Hong Kong and Shanghai – as well as elsewhere in China such as Shenzhen and Guangzhou – are explained in terms of 'win and lose'. That is, the increasing prosperity in Shanghai and Guangzhou is to the detriment of Hong Kong.

This is a very simple and flawed argument that overlooks the complementary, rather than competitive, roles that Hong Kong and Shanghai play, and the different focus of development in the Pearl River Delta and Yangtze River Delta.

The Pearl River Delta is much more externally-oriented economy than the Yangtze River Delta; services and flourishing private sector enterprises are the main economic drivers in the Pearl River Delta while the Yangtze River Delta has accommodated more heavy industry as well as the recent emergence of IT-related industry.

Hong Kong is and will remain the pre-eminent international financial centre for the entire Mainland, a major hub for regional headquarters in the Asia-Pacific and a growing centre of trade and investment for the fast-developing domestic economy in the Pearl River Delta.

Another often overlooked fact is that Hong Kong enterprises are the largest external investors in Shanghai and the Yangtze River Delta – in other words Hong Kong companies have been helping to fuel the rapid development of Shanghai and its hinterland while gaining benefits in the process.

Shanghai will continue to develop as the major financial and business centre for the domestic Mainland market, particularly the eastern seaboard, and as the major hub for industrial development in the Yangtze River Delta.

As an international financial centre, Hong Kong casts itself as the business, trading and services hub for the Mainland and the region as a whole. At the same time, Hong Kong and the Pearl River Delta will continue to be the main economic engine of southern China, as well as an increasingly affluent consumer market and a strong regional economy serving the global export market.

A Tale of Two Regions*

	GDP *(US$ billion)*	Exports *(US$ billion)*
Hong Kong	162.6	201.9
Pearl River Delta	258	289.1
Shanghai	55	25.4
Yangtze River Delta	185.4	47

**Figures for 2000*

Hong Kong's advantages

Hong Kong does have a number of advantages over other Mainland cities, and will continue to do so in the foreseeable future. These do factor heavily in the decision-making process of multi-nationals looking for a regional base, or of small and medium-sized enterprises looking for a foothold in the Mainland market or the Asian region.

The most important is Hong Kong's legal system, which is trusted, tried and tested by international business.

Hong Kong's capital account is fully convertible, and there are no restrictions on foreign exchange dealings. Property, securities, gold and silver can be bought and sold by anyone, without restriction.

A strong and well-regulated financial sector, a free press, the free flow of information, low taxes and a simple taxation system, a pool of managerial talent with international experience, ease of access, proximity to major markets, and a dense network of services firms are among the strengths and advantages of doing business in Hong Kong.

Specifically:

Services: About 86% of Hong Kong's GDP comes from service industries, compared to less than 35% on the Mainland. There will be a large shortfall of skilled professionals and services staff in China. Areas such as management, design and marketing, legal services, transport and logistics, finance and accounting services all correspond perfectly with Hong Kong's niche.

Access: Hong Kong has long been an entrepot for trade with the Mainland and is the key conduit for international trade with China. Around one-quarter of the Mainland's imports and 40% of its exports are handled through Hong Kong. More than 31 300 vehicles cross between Hong Kong and Guangdong daily, while over 313 000 people cross between China and Hong Kong daily by land, sea or air. There are about 1 000 flights a week between Hong Kong and 43 Mainland cities.

Financial centre: Predicted increases in FDI into China over the next five years will create great opportunities for Hong Kong's financial services sector – banking, fund management, insurance, underwriting, the debt market. Hong Kong's stock market, the third-largest in Asia after Japan and the Mainland, is considerably more liquid, and more familiar to investors, than Mainland stock markets. Many Mainland companies will look to raise capital in Hong Kong to fund business expansion or modernisation plans.

Experience: Since China opened its doors to the world in the late 1970s, Hong Kong companies have invested more time, money and resources than any others tapping the potential of the Mainland market. Hong Kong shares the same language and culture as China, and draws on more than 150 years of trading and investment experience in the Mainland. Hong Kong's small and medium enterprises have the know-how needed to do business successfully in China. More than 100 000 Hong Kong companies source products from China for the world market.

Low taxes: Hong Kong has low taxes and a simple taxation system. Corporate profits tax is 16%, while salaries tax is capped at 15%. There is no capital gains tax and no withholding tax.

Enhancing competitiveness

Hong Kong's long-term economic prospects hinge on being able to maintain competitiveness and relevance as a major centre for international finance, trade, transport and logistics, professional services, communications and tourism.

In the past five years, Hong Kong has been positioning itself to sustain reasonable economic growth in a rapidly-changing, knowledge-based world. Two serious economic downturns during that time, coupled with China's entry to the World Trade Organisation, have served to highlight the forces impacting on this goal.

Reforms have been launched in the key areas of financial services, education and the public sector to enhance Hong Kong's attractiveness as a business hub with a highly-skilled workforce and a small, efficient government.

Major initiatives have been undertaken to improve the environment, consolidate and augment Hong Kong's position as Asia's most popular tourist destination and to build the infrastructure needed to ensure continued development as a hub for trade and transport in Asia, and in particular the rapidly growing Pearl River Delta.

Concerted efforts have been taken to promote and position Hong Kong as Asia's world city. The Brand Hong Kong programme, launched in May 2001, is a long-term undertaking to focus greater international attention on Hong Kong's strengths and advantages as the most free, open and cosmopolitan city in Asia.

In July 2000, the government established a dedicated department – Invest Hong Kong (InvestHK) – to spearhead efforts to attract inward investment into Hong Kong. InvestHK actively promotes Hong Kong as the premier business hub in the Asia-Pacific region, and as the best location to access the enormous potential of the Mainland market. Partly as a result, the international business community has taken note of Hong Kong's advantages. Regional operations in Hong Kong rose to 3 237 by June 2001, an 8% increase over the 3 001 in June 2000 and a record high since the survey of regional operations began 11 years ago.

The major reasons companies were attracted to Hong Kong were low and simple taxes, the free flow of information, political stability and security, corruption-free government and excellent communications, transport and other infrastructure.

Boosting links with the Pearl River Delta

Central to Hong Kong's long-term success is greater economic co-operation and inter-dependence with the adjoining Pearl River Delta (PRD) hinterland.

The PRD has specific advantages and significant potential as a consumer market, a trading hub, a manufacturing base, a services market and as a destination for investment.

The PRD (including Hong Kong and Macau) is the fastest growing and most affluent region in China. It has a population of about 48 million, which is more than the population of Canada, or Taiwan and Malaysia combined. The PRD has a total GDP of US$258 billion – more than Switzerland, Sweden or Austria – which would put it amongst the world's top 20 economies.

Hong Kong has helped fuel the PRD's rapid growth and development over the past two decades. Hong Kong is the largest investor in the area, and there are more than 36 000 Hong Kong-linked companies employing more than five million people in Guangdong Province.

Hong Kong manufacturers are already the most active and experienced investors in all PRD cities, which make them ideal partners for foreign investors wishing to utilise the PRD's well-established manufacturing capabilities. Hong Kong's wealth of experience in the international trading arena also provides Mainland companies with a ready-made partner to expand operations for the global market.

Despite the depth and breadth of these links, there is a need to significantly boost cross-boundary co-operation to capitalise on existing strengths and synergies and maximize the area's potential, but in a way that preserves Hong Kong's unique advantages under 'One Country, Two Systems'.

The emphasis is on smoothing the flows of people, goods and capital between the Hong Kong SAR and the PRD's major cities, which include Guangzhou, Shenzhen, Zhuhai, Zhongshan, Dongguan, Foshan, Huizhou, Huiyang, Huidong, Zhaoqing, Jiangmen as well as Macau.

More resources will be devoted to hastening the flow of people and goods through such initiatives as co-located

Customs and Immigration checkpoints, the development of an electronic cargo clearing system and the opening up of new road and rail routes between Hong Kong and the PRD. There are plans for further co-operation in the logistics sector and to provide ferry services connecting the PRD's major port cities with Hong Kong International Airport. All these initiatives will enhance the export efficiency of the PRD region.

In July 2002, Hong Kong's first Economic and Trade Office in the Mainland will open in Guangzhou to promote economic co-operation and to strengthen business and economic liaison between Hong Kong and the PRD. A major reason for establishing the office is to help Hong Kong businesses to better understand the opportunities emerging in Guangdong following China's WTO entry. The office will also enhance understanding between the HKSAR and Guangdong governments, provide better support for Hong Kong businesses and promote investment in Hong Kong.

Infrastructure

A comprehensive strategic planning study – *Hong Kong 2030: Planning Vision and Strategy* – was announced in February 2001 to set out the blueprint for the development of Hong Kong over the next three decades.

The study aims to provide a planning framework for:

- Adhering to the principle of sustainable development, conserving the natural landscape and preserving cultural heritage
- Enhancing the hub functions of Hong Kong
- Providing a good quality living environment
- Meeting housing and community needs
- Providing a framework to develop a safe, efficient, economically-viable and environmentally-friendly transport system
- Promoting tourism
- Strengthening links with the mainland of China to cope with the rapid growth in cross-boundary interactions

The Chief Executive, Mr Tung Chee Hwa, announced in his Policy Address in October 2001 an ambitious infrastructure plan worth HK$600 billion (US$77 billion). Of this, one third would be spent on expanding the railway network to make it the backbone of Hong Kong's public transport system.

The investment plan also covers road, land and other construction works that will substantially enhance Hong Kong's quality of life, provide 21st century infrastructure and support the economic restructuring now taking place. In the process, new jobs will be created and significant business opportunities will be available for local and overseas companies.

Railways

From 2002 to 2007, six new rail projects costing US$13 billion (HK$100 billion) will come on line at a rate of about one a year. The existing railway network will be expanded by 40% to over 200 kilometres. Urban areas will be connected with new towns in the eastern and north-western part of the New Territories.

A second rail passenger boundary crossing at Lok Ma Chau will be developed to handle the substantial growth in two-way travel and commerce across the boundary. A dedicated rail link will be built to Hong Kong Disneyland, due to open in 2005.

Plans are being developed for another six new rail projects before 2016. These include a Port Rail line linking the container port at Kwai Chung with the railway network in the Pearl River Delta and a high-speed railway linking Hong Kong to Guangzhou via Shenzhen.

The expansion of the railway network is vital to meeting Hong Kong's increasing transport needs in a sustainable manner. It will also help the Pearl River Delta develop as an integrated regional economy bringing closer economic and social links between Hong Kong and the Mainland, particularly Guangdong Province.

Roads

Over the next decade, more than 100 kilometres of major trunk roads will be constructed and improved, including the Deep Bay Link and the Shenzhen Western Corridor. Total investment on these projects will be over HK$100 billion (US$13 billion).

The proposed Shenzhen Western Corridor will provide a strategic link between Hong Kong and Shenzhen across Deep Bay. It is an integral part of the infrastructure being put in place to provide more and faster cross-boundary links with the Mainland to expedite the flow of people, cargo and capital between Hong Kong and the Pearl River Delta.

Container Port

Container Terminal 9 (CT9), now being built on Tsing Yi Island by the private sector, will consolidate Hong Kong's position as the world's busiest and most efficient container port. The 68-hectare project will have six berths and a design capacity to handle more than 2.6 million twenty-foot equivalent units (TEUs) a year.

CT9 is expected to be completed in 2004, and will bring annual total capacity at the Kwai Chung Container Terminal Basin to more than 15 million TEUs. The new marine basin will be able to handle the largest container ships currently on the drawing boards.

Upgrading human capital

Whatever Hong Kong's aspirations, they can not be met without a broad, deep pool of talented people.

This can be achieved by providing a world-class education system in Hong Kong, and by attracting the best and the brightest from all parts of the world to live and work in Hong Kong.

A series of new education initiatives have been launched over the past five years to enhance the quality of education.

The focus has been to move away from the learning-by-rote system to one that provides children with a more well-rounded education that encourages curiosity and nurtures their own particular strengths and interests.

Considerable resources have also been committed to encourage Hong Kong people to continue learning throughout their lives. In his 2001 Policy Address, the Chief Executive, Mr Tung Chee Hwa, announced the establishment of a HK$5 billion (US$640 million) Continuing Education Fund to subsidise those with learning aspirations to pursue continuing education and training programmes.

There have been reforms and significant improvements in the areas of:

- Early childhood education (upgrading qualifications of kindergarten teachers);
- Curriculum development (providing teachers with greater flexibility to provide students with a comprehensive and balanced learning experience covering intellectual development, life skills, community services, work-related experiences, as well as physical and aesthetic development).
- School place allocation systems (reducing the incentive for unhealthy drilling in early childhood and primary education).
- Strengthening remedial and enhancement measures (helping all students to obtain basic standards, or talented students to pursue excellence).
- Public examinations (placing more emphasis on students' higher-order thinking skills and setting clearer assessment standards).
- Enhanced learning opportunities (increasing subsidised Secondary 4 and 5 places for those willing and able to continue studies).
- Increased resources for teaching English and Chinese, including Putonghua (introduce native English-speaking teachers and making Putonghua a core subject in secondary and primary schools, raising the language proficiency of English and Putonghua teachers).
- Upgrading the quality of teachers (percentage of trained teachers in public sector schools increased from 85% in 1997 to 91% in 2001).

Attracting talent

Hong Kong's liberal immigration regime has made it reasonably easy to attract and retain talented people from around the world. About 300 000 expat business people, professionals, personnel and their families live in Hong Kong.

However, more is being done in a number of areas:

- Reviewing immigration policy with a view to relaxing restrictions on the entry of overseas investors who wish to invest and live in Hong Kong without engaging in the running of the business.
- Securing agreement with Mainland authorities to extend the validity period of multiple business visit endorsements for Mainland business people from six months to up to three years, and extend the duration of stay to 14 days.
- Accelerating the entry to Hong Kong of Mainland people with skills or qualifications needed to help Hong Kong's ongoing development through an Admission of Talents Scheme and an Admission of Mainland Professionals Scheme.
- Making it easier for foreign nationals living in Hong Kong to visit the Mainland. The HKSAR Government secured the agreement of the Mainland authorities to issue three-year, multiple-entry visas to Hong Kong permanent residents who are foreign nationals. The new measures were introduced in December 2001.

Tourism

Despite two economic downturns in the past four years, and a global slowdown in tourist traffic after the September 11, 2001 terrorist attacks in the United States, Hong Kong's tourism industry has continued to record impressive growth.

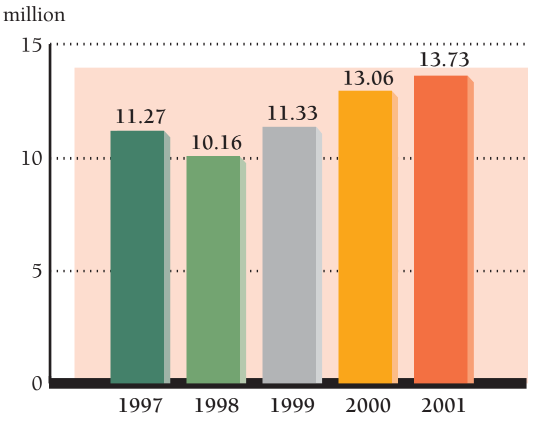
This growth has been fuelled by increasing numbers of visitors from the Mainland, and greater promotion of Hong Kong's attractions in other key markets.

The scrapping of a quota system for Mainland tour groups in January 2002 has provided a great boost to arrivals from across the boundary, as well as a fillip to tourism-related businesses such as hotels, restaurants and bars and retailers.

However, competition for visitors throughout the region is fierce and Hong Kong has been continually upgrading its tourism product to meet future challenges.

Part of the strategy has been to promote Hong Kong as a top-class destination for leisure and business visitors. This involves providing additional infrastructure, improving existing facilities, enhancing service quality,

Tourist arrivals 1997 - 2001



facilitating entry of visitors and active promotion overseas.

In the past few years, new attractions have been announced to enhance the drawing power of Hong Kong and to sustain the long-term development of the tourism industry.

In December 1999, a deal was signed with The Walt Disney Company to bring the magic of Disney to Hong Kong.

Reclamation work on the site at Penny's Bay on Lantau Island started in mid-2000 and is more than 90% complete. Infrastructure works commenced in October 2001.

Hong Kong Disneyland Phase 1 will include a Disney theme park, Disney-themed hotels and retail, dining and entertainment facilities. It will occupy 126 hectares, and can be expanded to 180 hectares in the future. Phase 1 is expected to open in 2005.

The project involves a total commitment of HK$22 billion (US$2.8 billion) in public funds (infrastructure, loans and equity). In its first full year of operation, Hong Kong Disneyland is expected to attract over 5 million visitors, including 1.4 million new tourists, and stimulate additional spending of HK$8.3 billion (US$1.1 billion). Over a 40-year period it is expected to generate economic benefits amounting to HK$148 billion (US$19 billion).

Many other projects are also in the pipeline. Plans were announced in 2001 to implement five major tourism clusters to broaden the range of tourist facilities in Hong Kong. These will be developed in the medium to long term:

- Yam O on Lantau Island will be developed into a new tourism node. This, together with Hong Kong Disneyland, the Tung Chung Cable Car and the Big Buddha will make Lantau Island a truly spectacular tourism area.
- The beautiful countryside and peaceful harbour at Sai Kung in the eastern New Territories will be carefully and sensitively developed to provide a range of active recreational facilities such as hiking and water sports together with world-class resorts.
- A culture belt will be developed to stretch from a new integrated arts, culture and entertainment district on the West Kowloon Reclamation to the existing museums and performing arts venues in Tsim Sha Tsui, the former Marine Police Headquarters and the Tsim Sha Tsui Promenade. A new tourism node will be developed at south-east Kowloon incorporating a large-scale multi-purpose stadium and a new cruise terminal capable of meeting the needs of the new generation of mega cruise ships.
- A heritage, entertainment and dining area will be developed in the heart of Central, radiating from the site of the existing Central Police Station and covering attractions like Government House, St John's Cathedral, Hollywood Road and Lan Kwai Fong.
- Ocean Park's strategic development plan will be supported to help it integrate into the new Aberdeen Harbour tourism node.

Apart from this, a major eco-tourism facility, the Hong Kong Wetland Park project is being developed near Inner Deep Bay/Mai Po in the far northwest of Hong Kong. This will showcase Hong Kong's ecological richness and complement the internationally recognised wildlife conservation area in the adjacent Mai Po Marshes. The project is due for completion in 2005.

Action is also in hand to improve existing tourist attractions and facilities. Since 2000, a district-based tourist enhancement programme was launched to upgrade existing tourist attractions. Visitors' signage covering all 18 districts is being installed and will be completed in 2003.

To promote quality service among the retail and catering sector, the Hong Kong Tourism Board (a statutory body responsible for marketing and promoting Hong Kong as a tourist destination) launched the Quality Tourism Service Scheme (QTS) in 1999. So far, more than 860 retail and food premises have joined the scheme with more than 2 900 outlets now eligible to display the QTS logo as a sign of their adherence to high service standards.

A public education campaign was launched in 2001 to promote a hospitable culture in the community. New legislation has been passed to regulate inbound travel agents and the trade will implement a training and certification programme for tour guides to ensure they have the appropriate skills.