

LEGISLATIVE COUNCIL BRIEF

Promotion of Inward Investment

INTRODUCTION

At the meeting of the Executive Council on 21 March 2000, the Council took note of the information set out below regarding the new strategy and institutional arrangements for the promotion of inward investment in Hong Kong.

BACKGROUND AND ARGUMENT

General Background

2. Foreign direct investment has long played an important role in the development of Hong Kong's economy. According to surveys conducted by the Government, at the end of 1997 foreign-owned firms employed about 18% of Hong Kong's total workforce. Foreign-owned manufacturing firms accounted for 35% of Hong Kong's total domestic exports.

3. Historically, the Industry Department (ID) operated an inward investment promotion programme to attract foreign investment to Hong Kong's manufacturing industries. Having regard to the structural changes in Hong Kong's economy, the scope of the investment promotion programme was expanded in 1996 to include service industries. Currently, the programme's objective is to promote and facilitate inward investment in Hong Kong's manufacturing and service sectors, thereby encouraging transfer of advanced technology and management expertise; to enhance the technology and productivity of local industries; and to promote the further development of Hong Kong as a regional and global service centre.

4. The investment promotion programme is carried out by the One-Stop Unit (OSU) of ID and the Investment Promotion Units (IPUs) of seven of the Government's overseas Economic and Trade Offices

(ETOs) in Brussels, London, New York, San Francisco, Toronto, Tokyo and Sydney. The seven IPU's are supervised on a day-to-day basis by the Heads of Overseas Offices (HOOs) concerned along the strategic direction set centrally in Hong Kong. Contacts with prospective investors are developed by IPU's through company visits, international fairs, exhibitions and seminars. The OSU in Hong Kong facilitates inward investors by providing information, identifying local business partners, and arranging visits and meetings.

Consultancy Study on Inward Investment

5. In view of the contribution of foreign direct investment to the development of our economy and the increasing competition for such investment in the region, it is imperative to ensure that the existing inward investment promotion programme continues to meet its public mission and is relevant to today's needs. We therefore commissioned in December 1998 a consultancy firm, PricewaterhouseCoopers, to evaluate and make recommendations on -

- (a) the best programme for promoting inward investment in Hong Kong; and
- (b) the most suitable institutional arrangement to deliver the programme recommended.

A Steering Committee chaired by the Trade and Industry Bureau (TIB) oversaw the study. The consultants submitted their final report in December 1999. The executive summary of the report is at Annex.

6. The study report has identified a number of weaknesses in our existing inward investment promotion programme and suggested that we should revamp our strategy as well as institutional arrangements in order to improve the effectiveness of our programme.

7. The key recommendations made by the consultants are as follows -

- (a) Strategy recommendation : Hong Kong should adopt a more proactive inward investment promotion strategy by -
- (i) focusing its promotional effort on a relatively small group of business sectors where Hong Kong can do well;
 - (ii) adopting a more proactive marketing approach with specific company targets;
 - (iii) strengthening “aftercare” service with a view to retaining and expanding investments already made; and
 - (iv) fostering "product" development to increase Hong Kong's attractiveness and competitiveness to prospective investors, especially in targeted sectors.
- (b) Institutional arrangements : A new organisation, in the form of either a government department or a stand-alone body, should be established to carry out the proposed new strategy. A private sector advisory group should be set up to provide input to the formulation of strategy and programme. Besides, an inter-bureau group should be set up to coordinate policy development and implementation.

Considerations

8. Our current investment promotion effort is based on an extensive, broad-based approach, in terms of both the number of markets/sectors covered and the number of company visits and promotional events undertaken. Moreover, until recently there has been a focus on manufacturing. While priority sectors are identified for promotion, the total number of such sectors amounts to some 20, and it is not unusual that each IPU will pursue about 10 priority sectors each year. As a result, in-depth and targeted promotion work is limited.

9. The current strategy was appropriate in the past when Hong Kong could still compete reasonably well on cost grounds vis-à-vis its neighbouring economies. In view of increased globalization and the shifting of comparative advantages, we agree with the consultants that promotion efforts based on an extensive and broad-based approach is not enough to ensure that we continue to stay ahead. The *objective* of our investment promotion programme should have a sharper focus and a closer alignment with the strength and development of our economy. At

the same time, we are acutely aware that whatever new strategies we seek to adopt should be consistent with our free market philosophy. Tools available to many of our regional competitors in attracting foreign direct investment, such as tax concession and free land, may not be suitable to Hong Kong.

10. We consider that general image building of Hong Kong overseas is necessary, and should continue to be an important pillar of the work of the ETOs. Where investment promotion is concerned, however, we agree with the consultants that Hong Kong should adopt a *more focused approach* by concentrating our effort on areas in which Hong Kong can do well. This will allow us to optimize the use of limited resources. This will also bring Hong Kong closer to international best practices.

11. As regards *target sectors*, the consultants have recommended five "primary" sectors, namely, regional headquarters/offices, financial services, trade related services, transportation services and telecommunication services, as well as four "secondary" ones, namely, business services, information technology (manufacturing and services), multi-media services and electronics (manufacturing). We are content with these recommendations *as a start*. These sectors are fairly broad and are closely associated with Hong Kong's existing strengths. Their continued inclusion in the target sector list should however be reviewed from time to time to take into account changing developments (please see para. 17 below). For these target sectors, not only will we carry out sector-specific general promotion work, but we will also target our effort at individual companies.

12. We agree with the consultants that *company targeting* should be carried out at two levels –

- (a) companies with no presence in Hong Kong but which have the potential to invest here; and
- (b) companies which have already invested in Hong Kong but which may either move elsewhere or be interested in expanding their investment here.

For the second category of companies, we agree with the consultants that a substantially enhanced *aftercare programme* should be put in place.

13. The consultants have emphasised the importance of providing adequate *resources* for the investment promotion programme. We agree that our promotional work needs to be enhanced by the provision of additional financial resources, redirecting resources to target sectors and greater specialization of human resources.

14. A focused approach would also require a review of the *geographical spread* of our investment promotion effort. The consultants have recommended that we concentrate on those markets with the greatest potential. We agree with the thrust of this recommendation, and will decide on this matter once the head of the new agency has been appointed and reviewed this matter.

15. As regards *non-target sectors*, we will continue to handle enquiries from prospective investors and provide them with the necessary support. There should be no question of their being given inferior treatment once we have learned of their interest. We should continue to ensure that Hong Kong will remain open to investors in all sectors.

16. We agree with the consultants that we should encourage *product development* aimed at improving Hong Kong's overall "offer" to potential investors, especially in target sectors. The "offer" that needs to be improved will depend on the sectors involved but common areas for improvement will likely involve the cost of doing business, availability of skilled labour, provision of land site, etc. We also share the consultants' view that establishing a financial incentive programme on an across-the-board basis will not suit Hong Kong well. As regards the need for tailor-made incentive packages on a genuinely exceptional basis to attract strategically important projects which will make a major contribution to Hong Kong's economic development, or "catalyst" projects to increase investors' awareness and interest, we believe that their exceptional nature dictates that each case has to be considered on its own merits against our long-held principle of maintaining a level playing field for all.

17. On *institutional arrangement*, we consider that the revamped investment promotion strategy should be appropriately backed up at both the policy direction and service delivery levels. Having regard to the consultants' recommendations, we will –

- (a) set up an inter-bureau group chaired by the Financial Secretary to oversee and coordinate policy making and implementation.
- (b) seek more proactively private sector input in drawing up the investment promotion programme. We intend to do so on a regular basis by leveraging on the expertise of the Business Advisory Group chaired by the Financial Secretary; and
- (c) set up a dedicated Government agency, to be named "Invest Hong Kong" and reporting to TIB, to execute our investment promotion programme. We have considered the possibility of setting up a non-government agency for the purpose. Given that investment promotion work will almost invariably require coordination of the work of different Government bureaux or departments and access to officials at senior levels, we believe that a Government agency would be more suitable. We intend to recruit to the agency relevant experts from the private sector to enhance the performance of its work.

FINANCIAL AND STAFFING IMPLICATIONS

18. The current inward investment promotion programme undertaken by the ID and the ETOs is operated at an annual recurrent cost of about \$70 million, of which about \$45 million is the staff cost of 51 staff. In addition, about \$16 million in capital expenditure is incurred annually for marketing and promotion. Implementation of the revised inward investment promotion strategy would require additional resources. The consultants have estimated that, on a conservative basis, an additional \$24 million in recurrent expenditure would be required and there should be suitable enhancement in capital expenditure on marketing. We have earmarked the necessary resources in 2000-01 for implementing the recommendations based on the consultants' estimates. We will work out the exact requirements taking account of the detailed institutional setup of the new agency and scope for rationalising current spending in

this area.

ECONOMIC IMPLICATIONS

19. Foreign direct investment helps foster Hong Kong's external trade, promote capital formation and create employment opportunities. It also facilitates technology and knowledge transfer, thereby upgrading technology in the economy and skills of the local workforce. The proposed initiatives will strengthen our capacity to promote Hong Kong as a destination for foreign direct investment, and thus will contribute towards Hong Kong's long-term growth as well as development into a knowledge-based and technology-driven economy.

PUBLIC CONSULTATION

20. Apart from discussions with relevant bureaux and departments, the consultants interviewed the Trade Development Council, chambers of commerce, foreign investors and broker agencies in the course of their study. We consulted the Services Promotion Strategy Group on the interim findings of the consultants.

PUBLICITY

21. The Financial Secretary announced the new strategy and arrangements in his Budget Speech on 8 March. The Secretary for Trade and Industry held a press conference on 10 March to elaborate on the changes. We will brief the Legislative Council Panel on Trade and Industry on the new arrangements. A spokesman will be available to answer media queries.

ENQUIRY

22. Any enquiries on this brief should be directed to Mr. Bobby Cheng, Principal Assistant Secretary for Trade and Industry at 2918 7460 or by facsimile at 2869 4420.

Trade and Industry Bureau
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