

HONG KONG STUDY

ANNEX M

EXTERNAL TRADE

Present Situation

1. Hong Kong is a major commercial centre within Asia and the world's seventh largest port. It has a free trade policy, and a sophisticated infrastructure. Hong Kong is almost entirely dependent on imported resources, including food and consumer goods. About 90% of its manufacturing output is exported, and domestic exports are equivalent to 60% of the Gross Domestic Product (GDP). The total value of visible trading transactions is twice the value of the GDP, and much more than this if invisible imports and exports are included.
2. Hong Kong has a free market economy. The Government sees its role not as planning the economy but as providing a suitably stable framework with minimum interference.
3. Although HMG have responsibility for external affairs in respect of Hong Kong, Hong Kong is allowed considerable latitude in external trade policy matters. Indeed it informally leads the group of major textile and clothing

/exporting

exporting countries opposing the EC's restrictive imports policy.

4. The PRC is a command economy and state trader.

General Agreement on Tariffs and Trade (GATT) and the Multi-Fibre Agreement (MFA)

5. GATT is both an international agreement setting out the ground rules for the open trading system and an international organisation which provides a forum for trade negotiations and for the settlement of disputes. Each Contracting Party to GATT has rights of access to other Contracting Parties' markets for its exports, and obligations in respect of access to its own market for their exports.

6. The MFA sets out special (and in principle temporary) provisions for international trade in low cost textiles. It is negotiated in the GATT and is in effect a derogation from normal GATT Rules. It provides a framework for an orderly world market in the products concerned, of which Hong Kong is by far the largest exporting country.

7. GATT is the cornerstone of Hong Kong's commercial policy. Hong Kong has GATT rights as if it was a Contracting Party by virtue of the United Kingdom's acceptance on Hong Kong's behalf. Hong Kong officials, accredited as members of the UK Mission, speak in GATT making it clear that they do so on Hong Kong's behalf.

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The UK signs GATT Agreements on behalf of Hong Kong. These include the MFA, although bilateral restraint agreements under the MFA between Hong Kong and individual importing countries are negotiated and signed by Hong Kong in its own right.

8. The PRC is not a Contracting Party to GATT. The Nationalist Government signed a Protocol of Provisional Application in 1948 but withdrew in 1950. According to the latest (1981) information, there is no immediate prospect of the PRC applying to join GATT, but their attitude may now become more positive: a request by the PRC to attend the GATT Ministerial meeting in November has been accepted by the Contracting Parties. But any application to accede, or (rather less likely) an attempt to 'reclaim the China seat', would be fraught with difficulties. The GATT is predicated on the assumption that the Contracting Parties are market economies. Special regimes have been imposed on those state traders (Poland, Hungary, Romania) which have negotiated terms for accession.

9. The PRC is not a signatory of the MFA either, but it attended the most recent round of renewal negotiations (end-1981) as an observer. It has a bilateral restraint agreement on textiles with the EC which is similar to, but in some respects more restrictive than, EC agreements with MFA signatory countries.

/Other

Other Agreements

10. Hong Kong is an associate member of ESCAP, and a member in its own right of the Asian Development Bank and the Asian Productivity Organisation. It is not separately represented in other international organisations. Hong Kong representatives in the UK Mission sometimes attend UNCTAD meetings but do not speak. International commodity agreements under the UNCTAD integrated programme apply to Hong Kong only by virtue of UK acceptance in respect of Dependent Territories as well as the metropolitan territory.

Hong Kong, China and the EC

11. Unlike other dependent territories Hong Kong was not included in, or associated with, the EC at the time of UK accession. It is treated by the Community as a third country with GATT rights. The PRC has a non-preferential trade agreement with the EC, guaranteeing that it is accorded the same treatment on tariffs as third countries with GATT rights (but see paragraph 12 below). However, like other state traders, it is still subject to discriminatory and (except in the textile sector) autonomously imposed quotas which the EC has given only a general undertaking to 'endeavour' to liberalise.

12. Under the EC Generalised System of Preferences Scheme (GSP), all non-associated developing countries benefit from reduced tariffs (in many cases zero) on their exports to the Community of all industrial and some

agricultural products. Use of the scheme by Hong Kong (but not China) is subject to special restrictions reflecting the territory's relatively high level of development and competitiveness. Other developed countries operate similar schemes, although on terms less generous than the EC's.

Hong Kong Trade with United Kingdom and China

13. In 1981, Hong Kong became the UK's biggest export market in Asia with UK exports reaching approximately £600 million (4.5% of Hong Kong imports and 1% of United Kingdom exports). But the visible trade balance remains in Hong Kong's favour at about £200 million in 1981. There were £4.8 million worth of United Kingdom exports to China via Hong Kong in 1980.

14. There is growing trade between Hong Kong and China. In 1981 21.3% of Hong Kong's imports came from China (its second largest supplier). 3.6% of Hong Kong's exports and 19.3% of Hong Kong's re-exports went to China.

Possible Changes

Recognition of Chinese Sovereignty with Continuing British Administration

15. Full British control involving responsibility for the conduct of Hong Kong's external relations (see Annex H) would enable Hong Kong to continue to benefit from its participation in international trading arrangements (eg GATT). This is a vital point for continued economic

/stability

stability. No compromise (eg Hong Kong's participation through the PRC) would maintain confidence.

16. Whether or not Hong Kong retains GATT status, Chinese bilateral trading agreements (eg with the EC, US and Japan) might theoretically apply to Hong Kong's external trade if Chinese sovereignty over Hong Kong is accepted. However, retention by HMG of responsibility for the conduct of Hong Kong's external relations would make it much more likely that the present arrangements would continue.

Hong Kong as a Special Administrative Region (SAR)

17. Under existing EC regulations, a range of sensitive products (including eg TV sets) are denied entry from China and there are annual quotas restricting the import of other products such as shoes. Textiles are the only Hong Kong products subject to EC quantitative restraints. If Hong Kong became a Chinese SAR, provided that British administration continued, it should be possible to argue in the EC that Hong Kong products should continue to benefit from the existing regime for access to the EC markets.

18. Among the other commercial issues that would need to be considered if sovereignty over Hong Kong passed to China are:

a) Export Credit

Hong Kong is ECGD's biggest single exposure, accounting at present for some £3.2 billions, little of which is

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covered by a Hong Kong Government guarantee. The predominant components of the total are the Castle Peak A and B power stations. ECGD's exposure on China is £216 million but could increase significantly, eg if the United Kingdom won a major share of the business on the proposed Guangdong nuclear power station. If Hong Kong became a Chinese SAR, with continuing British administration, the question of the degree to which China assumed responsibility for Hong Kong's existing and future debts would be a question for future negotiation when and if China resumed full jurisdiction.

b) Strategic Export Controls

China, but not Hong Kong, is at present subject to COCOM strategic export controls. How far it would be possible to continue this with a SAR solution would require careful consideration. Obviously the Chinese will oppose it.

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A SPECIAL STUDY

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FUTURE OF HONG KONG

SPECIAL STUDY

Contents

Paragraph No.

MAIN PAPER

PART I

The Problem	1
British Interests	6
The Chinese Position	8
Interests of the People of Hong Kong	12

PART II

Strengths and weaknesses in the British and Chinese Positions	14
Time Factor	18
Impracticable Options	20

PART III

British Aim	21
Possible approaches to the problem of sovereignty	22
A possible solution	26
Detailed Studies	31
Conclusions	33

PART IV

Recommendations for the Prime Minister's visit to Peking	34
Public Presentation	44

Contents (continued)

ANNEXES

- A. Treaties of 1842 and 1860
- B. Convention of 1898
- C. Map showing the New Territories
- D. Chinese Proposals on Taiwan
- E. Consultation in Hong Kong
- F. Options for Solution and Legislative Requirements
- G. Constitutional Position of Hong Kong
- H. External Relations
- I. Currency and Finance
- J. Defence and Internal Security
- K. Citizenship, Nationality and Immigration
- L. Legal System
- M. External Trade
- N. Civil Aviation and Shipping
- O. Crown Land Leases in the New Territories
- P. Illustrative Questions and Answers following the Prime Minister's Visit to China



PRIME MINISTER
FIRST LORD OF THE TREASURY

FUTURE OF HONG KONG

SPECIAL BRIEFING

To Be Retained
Do Not Destroy

FUTURE OF HONG KONG

LIST OF BRIEFS

1. Introduction. Tactics
2. Labour Government Statements on HMG Commitment
3. Draft Press Statement on Hong Kong
4. Draft Aide Memoire
5. Chronology of Major Events and Statement
6. Draft Opening Statement
7. Form and Structure of Negotiation
8. Further Defensive Points
9. Possible Acceptable Package
10. Possible Concession which might be made during negotiation
11. Possible Chinese objections and suggested responses
- 11a. Answers to Criticisms Chinese Leaders may make
12. FCO Special Study
 - (a) Treaty of Nanking 1842
 - (b) Text of Second Convention of 1898
 - (c) Map of New Territories
 - (d) Chinese Proposals on Taiwan
 - (e) Consultation on Hong Kong
 - (f) Options and Solution and Legislative Requirements
 - (g) Constitutional Position of Hong Kong
 - (h) External Relations
 - (i) Currency and Finance
 - (j) Defence and Internal Security
 - (k) Citizenship, Nationality, Immigration
 - (l) Legal System on Hong Kong
 - (m) External Trade
 - (n) Civil Aviation and Shipping
 - (o) Crown Land Leases in New Territories
 - (p) Illustrative Questions and Answers Following Prime Minister's Visit to China.