
II. *The Economy*

A. Strategies for Growth

19. To help our economy respond to the changes I have described, our strategy will be to focus on increasing the diversity of the economy by creating conditions for growth in sectors with a high value-added element, in particular in those industries which place importance on high technology and multi-media applications. We will also encourage businesses to take advantage of the opportunities offered by the Mainland, and we will bolster the established pillars of our economy such as the financial services sector, small and medium enterprises, tourism and import and export. We must also upgrade the skills of our workforce. As our strategy unfolds and we regain economic momentum, we will look forward to more opportunities for our citizens and a better employment environment.

Innovation and Technology

Engines of Growth

20. Innovation and technology are important drivers of economic growth. In a knowledge-based global economy, they are essential in adding value, increasing productivity and enhancing our overall competitiveness. The world's most outstanding economic success stories of recent years have mostly involved the application of innovation and technology. In the world's largest economy, that of the United States of America, 80% of productivity growth is attributed to technological and knowledge-based advances. This is not a phenomenon unique to the biggest economies. For example, Israel's high-tech exports in 1997 represented two-thirds of the country's total exports and were worth nearly HK\$70 billion - double the 1990 figure. To achieve success in this area however does require a dedicated effort and a commitment to investing in the necessary technological infrastructure, which includes research and development, support to industry and human resources. Although the rewards may not be immediately apparent, this is an essential investment in our future.

21. Over the years we have steadily built up our technology sector. Our universities now spend some \$3.2 billion annually on research. We allocate \$180 million annually to the Hong Kong Productivity Council which provides technical advice to industry. We have established the Hong Kong Industrial Technology Centre to provide services and support to industry to enhance technological development at a cost of \$250 million. We have injected \$750 million working capital into the Applied Research Fund and \$278 million into the Industry Support Fund to encourage innovation and support the development of new industries. In addition, we will build the first phase of the new Science Park in Tai Po, due to open in 2001, at a cost of \$3.3 billion. This will enhance our technological infrastructure.

22. These initiatives reflect the fact that the Government has done a lot to promote technological development. We now need to look critically at these initiatives and redefine our goals and objectives in the area of innovation and technology as a whole. I believe that a focused approach in this field, together with our sophisticated capital-raising markets, our rich market experience and our well-established international business links, will provide us with the potential to turn innovative ideas into commercial products on a far greater scale than at present. We need now to strengthen our support for technological development, build up a critical mass of fine scientists, engineers, skilled technicians and venture capitalists, and encourage the development of a significant cluster of technology-based businesses.

23. With all this in mind, earlier this year I invited Professor Tien Chang Lin to chair the Commission on Innovation and Technology. In its first report to me, the Commission recommends that, to realise our vision for Hong Kong to become an innovation and technology centre for South China and the region, we need to position ourselves to be -

- a leading city in the world for the development and application of information technology, especially in electronic commerce and software engineering;
- a world class design and fashion centre;

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- a regional centre for multimedia-based information and entertainment services;
 - a world centre for the development of health food and pharmaceuticals based on Chinese medicine;
 - a leading international supplier of high value-added products and components in areas where Hong Kong already excels today;
 - a regional centre for supplying professional and technological talents and services; and
 - the market place for technology transfer between the Mainland and the rest of the world.

24. To take forward these recommendations, it is essential that we have a clear policy objective, namely, to enhance the capability of our firms to innovate, and to stimulate technological development and encourage its commercialisation and application in Hong Kong.

Initiatives

25. To ensure that technological research can add the highest degree of value to economic activity, all the links in the research and development chain must be in place. The Commission has identified “mid-stream” research and development as an area of weakness in Hong Kong. Mid-stream research is a pivotal step between basic scientific research and its commercial application. To support and stimulate mid-stream research, I accept the Commission’s recommendation to establish an Applied Science and Technology Research Institute. In addition, to finance specific projects which will contribute to innovation and technological upgrading in our manufacturing and service industries, we will set up an Innovation and Technology Fund with an injection of \$5 billion.

26. This upgrading of our technological infrastructure will provide the basis for taking forward other important recommendations of the Commission. One is that we stimulate the collaboration of academic

institutions and industry in research and development. We shall do this by, for example, awarding matching grants for co-operative research between tertiary and other institutions and industry. Another recommendation is that we strengthen our industries' links to the technological institutes on the Mainland to make best use of the Mainland's research strengths and turn them into commercial products. In order to build a critical mass of expertise, we will consider measures which will enable employers to recruit the best professionals from the Mainland and elsewhere in the world. We will also more vigorously promote technological collaboration through various fora.

27. We are setting out on an important strategic course. The Government will do its utmost to provide an environment conducive to the development and application of innovation and technology, and I look forward to receiving in mid-1999 the Commission's final report, which will contain recommendations for moving forward on all fronts. We will study all these recommendations carefully, and will consider how to take them forward so as to create a favourable environment for business, in which we hope the private sector will capitalise on the opportunities which we seek to create. Certain industries in particular rely on advances in innovation and technology, and these sectors provide obvious scope for developing or further enhancing our competitive edge.

Information Technology

28. Hong Kong is among the world's most sophisticated users of IT, and the average growth rate in this industry in recent years, amounting to 23.5% annually, reflects its importance both in helping us to retain our competitive edge and in driving our overall economic expansion. We need to continue to make the best possible use of IT as an essential tool in speeding the flow of business and other communications. We also need to ensure that the IT industry can flourish in an environment which will encourage the creation of new products through innovation.

Internet Hub

29. With our excellent telecommunications infrastructure, our unique position vis-à-vis the Mainland and our bi-lingual language capability, Hong Kong has a strong competitive advantage in seeking to serve as an information gateway to the Mainland. Working with our Mainland counterparts, we will improve our mutual Internet links, making it easier for Hong Kong companies to integrate their manufacturing and supply operations on the Mainland. In linking the Mainland through Hong Kong to the rest of the world we will also be able to act as a digital intermediary, which will allow us to stimulate economic growth.

Electronic Service Delivery

30. Within Hong Kong, creating an infrastructure for the free flow of electronic transactions in the community will help promote the development and growth of new IT products and services. The Government will spend \$173 million on launching the on-line Government Electronic Services Delivery Scheme, which from 2000, will allow anyone to access public services and information 24 hours a day via the Internet and other means of electronic access. This will be an important step in facilitating growth in electronic commerce, as well as enhancing Government's own efficiency.

Broadcasting and Telecommunications

31. Two of our largest technology-intensive industries are broadcasting and telecommunications, which together have grown by some 14% annually in recent years. We aim to speed up growth in these industries, and therefore our economy, by creating the best possible market conditions and regulatory environment for investors in these sectors. Innovation and improvement in these industries will also lead to better service delivery and greater consumer choice, thereby promoting growth and creating new jobs.

32. In the coming year we will undertake two projects which will extend the frontiers of technology in Hong Kong's commercial broadcasting and telecommunications sector, namely -

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- technical trials of digital terrestrial television services; and
 - the development of a world class teleport at Chung Hom Kok to provide the best possible global satellite communication links.

We will also encourage greater investment and promote the provision of better services to the public in the television and telecommunications sectors by ensuring fair competition among service providers.

The Film Industry

33. Hong Kong's film-makers have long had a reputation for their distinctive style. Even today, when the industry faces difficulties, Hong Kong is still one of the world's major film producers. With a potential audience of over a billion people in the world-wide Chinese community alone, and the availability locally and on the Mainland of world-renowned creative and artistic talent, we see potential for further growth in our film industry. But the global film business is highly competitive, and our industry must upgrade itself if it is to capture a larger share of the market.

34. Government's role in this process will be to help provide an environment conducive to long-term development. In the past year we have set up a Film Services Office to help the industry with production and location shooting in particular, and provided a site for a state-of-the-art film studio with advanced post-production facilities. To help our film industry keep pace with new technology and skills, we propose to set up a \$100 million Film Development Fund in 1999. This Fund will promote innovation by supporting projects aimed at enhancing the industry's professional and technological capabilities; stimulating the growth of creative productions; facilitating the use of advanced special effects techniques; and improving the skills of employees. Some of the most successful films of recent times have relied greatly on computer graphics, and our overall investment in technology will also greatly enhance our capabilities in this area. I look to the film industry to make the best use of these favourable conditions to develop the industry.

Chinese Medicine

35. In last year's Policy Address I affirmed my belief in Hong Kong's potential to become an international centre for Chinese medicine and medical practitioners. This is another industry which, through the application of innovation and technology, can enhance our economic growth and give us a competitive edge on a global scale.

36. To provide for a regulatory structure for facilitating the use, trading and manufacture of Chinese medicine, and to recognise the professional status of Chinese medical practitioners, we will introduce the Chinese Medicine Bill into this Council in 1999. Registration of Chinese medical practitioners will begin in 2000. To encourage innovation and development in this field, in the past year we have funded a series of research programmes in our universities. We will now examine the case for establishing an Institute for Chinese Medicine which will focus on applied research. This will strengthen our scientific and technological base, and will facilitate the commercialisation of medicinal products.

Intellectual Property Rights

37. If Hong Kong is to become an innovation centre we must respect intellectual property rights. The Government is committed to upholding a world-class intellectual property rights regime. Our approach has been to maintain a comprehensive legal framework, to take vigorous and sustained enforcement action, to step up education and publicity and to create strong links with cross-boundary and international enforcement authorities as well as relevant industries. In the coming year we will devote extra resources to combatting illegal activities in this area and further increase our efforts to educate the public. We simply will not tolerate the theft of ideas, and I urge everyone in Hong Kong to support this effort by refusing to buy pirated or counterfeit goods of any description.

B. Building on Our Strengths

38. While we expand our economic horizon, we must continue to build on our existing strengths to ensure our long-term economic vitality.

Financial Services

39. Let me here state that Hong Kong is determined to maintain its position as the international financial centre of Asia and the key source of foreign capital for China. In past years the financial services sector has contributed substantially to our economy and will play an important part in our future. The current pressures in the Asian region may cause some economies to become more inward-looking, but Hong Kong will retain its free and open financial services structure. Furthermore, as China's economy develops and her need for foreign capital increases, Hong Kong's position as a major market for raising capital will become stronger.

40. We must now take a strategic view of what needs to be done to ensure that our financial market can support this expansion of our role. We will study, for instance, how best to use information technology to facilitate fully automated and seamless transactions in the market. We will provide the necessary regulatory framework to protect the integrity of the market. Recent experience has shown us how important it is to co-ordinate more effectively surveillance and regulation across all sectors of the financial services market. I have asked the Secretary for Financial Services to take a more active role in co-ordinating regulators and market operators, and to review the resources he needs to do this.

41. A robust market structure needs the support of a workforce with the ability to adapt to the challenges and opportunities ahead. I look forward to receiving recommendations from the Steering Committee on the Feasibility Study on the Financial Services Institute, which is currently examining human resources demand in this sector with a view to meeting tomorrow's needs for top-quality personnel. The Steering Committee is due to submit its recommendations in mid-1999.

42. We will also press ahead with the development of new services. We will study proposals for a Venture Board for smaller and emerging technology companies' stocks. To strengthen our role as an international financial centre, we will also continue to develop the debt market. The expansion of the Mortgage Corporation's business and portfolio and the introduction of the Mandatory Provident Fund Schemes will add impetus to this development.

43. Given sustained expansion and hence demand for capital on the Mainland, as well as the recovery of our economy, I expect the overall size of our stock market to increase as the current global financial uncertainties recede. I firmly believe that we will in the future strengthen our position as Asia's leading international centre for financial services.

Tourism

44. Our tourism sector is another one of our traditional economic strongholds. Hong Kong is the most frequently visited city in Asia. Tourists come here for the same reason they go to Paris, to Istanbul or to Rio de Janeiro - there is nowhere else like it. We have a unique flavour to our city, and visitors have long been attracted by our East-meets-West culture, our day and night shopping and entertainment, and a spectacular, yet safe physical environment. But past achievements are no guarantee of success in the future. Tourists now demand more sophisticated attractions, and our competitors in the region are upgrading their tourism infrastructure in a bid to capture a greater market share. We must therefore take a strategic view of how best to respond to the present circumstances, and develop initiatives to maintain the interest of visitors from the Mainland, from other Asian countries and from the rest of the world.

45. In order to enhance our appeal as a tourist destination, we will promote new attractions which will complement our unique flavour and provide for a wider range of events in Hong Kong. Our broader vision is to cultivate Hong Kong's image as the Asian centre of arts and culture, and of entertainment and sporting events. We need to build on the popularity of regular international events such as the Hong Kong Arts Festival and the

Rugby Sevens, as well as capturing the imagination with more cultural and artistic presentations such as the Treasures of China exhibition, which was so successful late last year.

46. I realise that this cannot be done without proper venues for world-class events. The Government is committed to providing more support in this area, and as a catalyst for upgrading our image as Asia's entertainment capital we are planning for a new, state-of-the-art performance venue on the West Kowloon reclamation. We will further develop proposals for other major facilities which will be both unique attractions in themselves as well as venues for cultural, entertainment or sporting events, including a new sports stadium, a new centre for water-sports and a multi-media theme park.

47. New facilities and attractive events are key planks in the tourism strategy, but they are not the whole story. We need also to look at ways of better presenting to the world our distinctive heritage, much of which is on show in our historical buildings and our archaeological sites, some of which date back 6 000 years. We intend to do more to promote our heritage to help develop tourism, and I have asked the Hong Kong Tourist Association to set up a Heritage Tourism Task Force comprising experts in this field. The Task Force will focus on individual initiatives and on a broader strategy for promoting our heritage sites and developing opportunities for joint promotions with the Mainland and other regional destinations.

48. To take our new vision for tourism forward with a clear focus, I have decided to appoint a Commissioner for Tourism whose duty will be to promote the development of this industry.

Small and Medium-sized Enterprises

49. Hong Kong's small and medium-sized businesses employ some two-thirds of the workforce and are the basic building blocks of our economy. With their relatively low start-up costs and flexibility in a changing business environment, small and medium-sized enterprises (SMEs) are a significant force in a renascent economy and create a large number of employment opportunities.

50. To ease the impact on our SMEs of the credit squeeze and provide them with working capital, we have established a \$2.5 billion Special Finance Scheme. This helps them secure loans from financial institutions, with the Government providing guarantees for loans. The Scheme has been in operation for six weeks, and as at the end of September, 92 companies had obtained loans amounting to \$176 million under the Scheme. There have been suggestions that the terms and conditions of the Scheme should be more flexible. We are monitoring feedback from SMEs, lending institutions and other interested parties, and we will review the Scheme early in 1999 to decide whether and how improvements need to be made.

51. SMEs often need help in certain key areas if they are to grow. These areas include: obtaining working capital, sourcing market information, finding good quality staff and controlling costs. We already have a comprehensive range of programmes to support SMEs, which are provided through the Industry Department and other institutions. For example, the Hong Kong Trade Development Council focuses on opening up overseas markets; the Vocational Training Council is geared towards human resources training and development; the Hong Kong Productivity Council works on productivity enhancement; and the Hong Kong Industrial Technology Centre helps nurture business ventures in technology. To strengthen the co-ordination and development of these and other available services and to help ensure that SMEs can make the best use of these services, we will set up a Small and Medium Enterprises Office within the Industry Department. We will also continue to fund projects which contribute to the development and competitiveness of our SMEs, such as those which relate to Year 2000, ISO 9000 application, manufacturing resource planning and technical assistance on environmental compliance, through the Industrial Support Fund.

The Manufacturing Sector

52. For many decades the manufacturing sector has contributed greatly to our growth. Although the 1980s saw a major move of labour-intensive production facilities across the boundary to the towns and cities of the Pearl River Delta, and indeed to other parts of the globe, we remain an active centre for the whole process of sourcing, distribution and other manufacturing

related services. Our flexibility and market knowledge help put us in the forefront of global production. This economic activity has also made Hong Kong the primary logistic hub for obtaining banking, insurance and transportation services, and has led to us becoming the home of the world's largest container port.

53. The quick response time and sophisticated workmanship of our manufacturers ensure that we maintain a manufacturing sector. Our traditionally important textile and clothing industry is still at the heart of this sector. Continued development of the manufacturing sector must be a matter of priority for our community as well as Government. Our push towards greater use of innovation and technology will help industries in this sector to expand and improve their production capabilities and ability to develop new products. For our part, we will help our manufacturers by, in our regular contacts with Mainland authorities, pursuing measures aimed at improving the environment for businesses operating in the Pearl River Delta.

Investing in Infrastructure

54. A continued investment in upgrading and expanding our physical infrastructure is essential if we are to improve our living environment, create more land for future use and stimulate the economy and provide jobs.

Aviation

55. Our public works programme is well-stocked with major projects aimed at improving our transport links, the most notable of which in recent years has been the new airport. The opening of the airport in July was not trouble-free. A Commission of Inquiry into the reasons for the early problems in the airport's operation is due to report to me in January next year, and I will act as appropriate upon the recommendations of that Commission.

56. Hong Kong International Airport is now processing some 80 000 passengers and 4 500 tonnes of cargo daily. About 80% of flights are departing within 15 minutes of scheduled time. Upon completion of the second runway the airport's capacity and operating flexibility will increase

further. It is indisputable that Hong Kong now has a magnificent new facility capable of allowing us to expand our air links and services for generations to come. The Airport Authority will keep under regular review the need for additional facilities and the Civil Aviation Department will begin work on converting our ground-based air traffic control systems to next-generation satellite systems. This will ensure that Hong Kong's civil aviation sector maintains the high standards expected of a major international aviation centre.

Local Transport Networks

57. To ensure that our transport system matches our development, we shall continue to build on our major road and rail networks. In my 1997 Policy Address I described some of our plans to expand these networks, and I am happy to report that we have made good progress in this area.

58. The planning and implementation of the priority railway projects are proceeding at full speed. Construction of the West Rail Phase I has been authorised and will start before the end of this year. We will seek authorisation for the MTR Tseung Kwan O Extension in the coming weeks so that construction work can also begin on this project before the end of the year. We aim to complete the necessary statutory procedures and finalise our planning for the implementation of the Ma On Shan Railway in 1999 so that construction can start in 2000. Altogether these railways, which will open between 2002 and 2004, will cost \$110 billion, and will create 27 000 jobs during their design and construction phase. To meet cross-boundary traffic demand, we are also planning to build a spur line which will connect the KCR at Sheung Shui with Lok Ma Chau, for completion in 2004.

59. As for major roads, we are making good progress with the design of the following projects which we are due to start building between 2000 and 2004 -

- Route 9 connecting Tsing Yi and Cheung Sha Wan;
- Route 16 connecting Sha Tin and West Kowloon;

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- the section of Route 5 connecting Tuen Mun Road and the Tsuen Kam Interchange; and
 - the section of Route 10 connecting North Lantau and Yuen Long.

The design and construction of these roads will create about 10 500 jobs. In addition, we have already made a start on preliminary planning for the Central Kowloon Route and Route 7 between Kennedy Town and Aberdeen. All these new roads will help to clear existing bottle-necks, as well as serve transport demand and tie in with land use planning.

60. Apart from these commitments, in 1999 we will complete the Second Railway Development Study and the Third Comprehensive Transport Study. These will provide us with a blueprint for road and railway expansion to meet transport and development needs to the year 2016.

Delivery of the Programme

61. It is understandable that in the current economic climate some might question our capacity for funding major new projects. We have examined again the level of our resources, and I can give this assurance: we have sufficient resources within our expenditure guidelines to allow us to realise the projects for which we have ear-marked expenditure over the next five years. Investing in high quality infrastructure is an investment in our future.

62. Our willingness to invest must be matched by an ability to deliver projects on time and within budget. The time required for a major project could be some 10 to 12 years from conception to completion. The necessary tasks of feasibility study, public consultation and land acquisition often take more time than the construction process itself. We will look for ways to shorten the time taken to complete these tasks. We are determined to minimise the cost of each and every project and to maximise cost-effectiveness. In assessing project cost we will have particular regard to the current downward trend in construction costs.

Anchoring our Fundamentals

63. I have outlined here some of the key steps we will take to improve the economic climate, based on a commitment to maximising our use of innovation and technology and on a pledge to build on our traditional strengths. The Government will work hard to achieve the objectives I have described. But the measures we will take to stimulate growth can only take root if grounded in a stable foundation. The most important fundamental element underpinning our future progress is the continual implementation of the “One Country, Two Systems” concept, in accordance with the Basic Law.

64. It is essential that we all re-affirm our commitment to preserving these fundamentals, which are the basis of our success. I would like to state clearly that the Government will uphold the rule of law and protect the independence of the Judiciary; guarantee freedom of speech and of the press, and facilitate access to information; continue to manage our economy on a free-market basis within a regulatory framework which creates a “level playing-field” for investors; maintain a strong stance against corruption; emphasise the importance of law and order; and preserve the international character of Hong Kong.

65. One of the reasons for Hong Kong’s success is that citizens of so many nations have made their homes here. The expatriate community contributes greatly to our economy and to our unique culture. We are determined to make this community more welcome in Hong Kong, and to remain the city of choice for multi-national companies wishing to establish a base in the Asia Pacific region. Recent figures show that 935 non-local companies, including some of the world’s largest financial institutions have their regional headquarters in Hong Kong. To reinforce our links with the international community, I have appointed a Council of International Advisers, whose members include prominent personalities in the fields of finance, commerce and industry from all over the world. This Council, which will help the Government broaden its international commercial perspective will hold its first meeting in Hong Kong in January 1999.

66. Our budgetary policy will continue to reflect the principle of fiscal prudence, ensuring that growth in government expenditure will be in line with medium term economic growth trends. Such financial discipline has been a cornerstone of our success, and has allowed us to build up strong reserves, which are essential to the protection of our linked exchange rate. In the current year, because of the contraction in the economy and the suspension of land sales, our budget deficit may be substantially more than the \$20 billion we announced in June. Because of the downturn in our economy, in the medium term our recurrent expenditure may grow more slowly than before. Nonetheless, we have the means to support our commitment to spending over the next five years in key areas such as infrastructural development, which are essential for our economic growth and which will create more jobs for our workforce.

67. Another element fundamental to our continued economic stability is the linked exchange rate. I will take the opportunity again today to underline our resolve to maintain our linked rate. Without it we would run the risk of major capital outflows, even higher interest rates and a crisis of confidence in our currency. It is an essential plank in our platform for growth, and will remain so.